

**STRATEGIC PETROLEUM RESERVE: A CLOSER
LOOK AT THE DRAWDOWN**

HEARING
BEFORE THE
SUBCOMMITTEE ON ENERGY AND POWER
OF THE
COMMITTEE ON COMMERCE
HOUSE OF REPRESENTATIVES
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THURSDAY, OCTOBER 19, 2000

HOUSE OF REPRESENTATIVES,
COMMITTEE ON COMMERCE,
SUBCOMMITTEE ON ENERGY AND POWER,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:10 a.m., in room 2123, Rayburn House Office Building, Hon. Joe Barton (chairman) presiding.

Members present: Representatives Barton, Stearns, Largent, Burr, Shimkus, Pickering, Boucher, Markey, and Wynn.

Also present: Representatives Tauzin and Green.

Staff present: Cathy Van Way, majority counsel; Miriam Erickson, majority counsel; Robert Simison, legislative clerk; Peter Kielty, legislative clerk; and Rick Kessler, minority counsel.

Mr. BARTON. The subcommittee will come to order. If our witnesses and our participants would find their seats.

I want to welcome everyone to today's hearing on the drawdown of the Strategic Petroleum Reserve.

The last hearing on September 28 dealt with natural gas and heating oil. We spent some time discussing the just-announced administration decision to release oil from the Strategic Petroleum Reserve. At that hearing, I questioned the authority for this action, the timing so close to the election, the cost of establishing such a dangerous precedent and whether it would actually accomplish the goal of increasing heating oil supplies to the Northeast.

Shortly after the hearing, I and Chairman Bliley wrote Energy Secretary Richardson and the President a letter expressing our concerns and asking for their responses to a list of questions. I am pleased to announce that the Department did partially respond and only 1 day late, which for them is pretty good work.

I am not satisfied with those responses. I don't think they were totally sufficient to the questions that were asked, but they said they would get us additional information. We will review their responses and probably ask for additional material.

The administration has begun to implement its program to release 30 million barrels of oil in what it calls a swap or an exchange. At the time the DOE announced this decision, they made public statements, sent out press releases that the purpose of the program was to avert a shortage of home heating oil. We now find out that, while heating oil supplies are lower than they normally should be expected, that no one is claiming there is a shortage.

Today we will examine the program as it is being implemented and see if it has any ability to implement the goal that it has announced. We will deal specifically with the mechanics of the program, policy issues involved in the decision and the impact of the action.

It appears that the administration has decided to make the Strategic Petroleum Reserve a focus of their energy policy, so we should discuss many of the issues that have been raised by the drawdown. It is questionable in my mind whether the President or the Department has the statutory authority to release the oil in this manner for this purpose. The Energy Policy and Conservation Act requires a severe supply disruption before drawing down the Reserve. Not only has the administration not informed the Congress of such a disruption, Secretary Richardson recently announced there was no energy crisis.

I also question the Department's characterization of this program as an exchange or swap, when its real purpose, and admittedly so, has been to increase the available amount of home heating oil in the marketplace. A variety of expert opinions question the release of 30 million barrels of oil will have any significant impact on home heating oil supplies. DOE itself estimates that it will increase home heating oil supplies by about 3 to 5 million barrels, and that is a very questionable assumption which we will get into in the hearing.

Third, some Members of the Congress have raised questions about the fact that heating oil made from the crude oil released from the Reserve could actually be exported outside of the United States.

Finally, many news reports have raised questions about DOE's governance of the bidding in the solicitation process. Simply put, in my mind the mechanics of this program are very flawed. The administration originally opened bidding to almost anyone without requirement that the bidders prequalify and demonstrate expertise in refining or trading or even promise to refine the oil here in the United States.

As it happened, 7 million barrels were awarded to bidders who could not live up to their end of the deal. Seven million other barrels have apparently been "flipped", meaning that the winning bidder simply sold to someone else and made a quick profit. Meanwhile, market analysts keep decreasing the amount of heating this release of unrefined crude oil will generate for the United States.

It is worth noting that the administration has changed its policies for the rebidding of the oil turned back in.

I will also point out that we have 2 million barrels of home heating oil in a Northeast Home Heating Oil Reserve. Unless the administration announces today they intend to release some of this home heating oil, the Reserve that was created specifically for the purpose that allegedly this program has been initiated is not going to be used this winter.

Nobody wants consumers in the Northeast or anywhere else to go without heating oil or to pay a higher than necessary price. We should be focusing on ways to help that situation.

As I just pointed out, millions of gallons of home heating oil are ready to be transported, are already in the Northeast but are not

being released. We also have millions of gallons of heating oil ready to be transported to the Northeast from the Gulf Coast, but they cannot find an American flag carrier to carry them.

The Federal Jones Act requirements prevent foreign flag ships from getting American heating oil where it needs to go, to the Northeast. The administration has some authority to waive the Jones act, and I have not heard that that is being considered.

To remedy this purpose, I have introduced legislation to grant a temporary waiver so any ship could carry heating oil to the Northeast. H.R. 5485 would provide a 90-day waiver of the Jones act, just this winter, for the transport of crude oil or refined products like home heating oil to any two ports selected by the President of the United States.

This bill is not in our subcommittee's jurisdiction, unfortunately, but it is the kind of more targeted action we must consider as a Congress and as a Nation. I am going to ask the leadership in the House to consider putting this bill on the suspension calendar next week so that we can move it to the Senate before we adjourn.

As I said in our last hearing, American consumers deserve a national energy policy that is comprehensive, long-term and well-integrated. The Strategic Petroleum Reserve is but a small part of a comprehensive U.S. energy supply equation. True leadership would see this recent increase in energy prices as a wake-up call and seize the opportunity to develop an overall long-term energy policy to serve the needs of the entire United States. Instead, the Clinton-Gore Administration apparently intends to rely on the Reserve as a tool to manipulate for their own political purposes.

At best, it is a short-term fix to a long-term problem. At worst, it could actually be counterproductive and give the American public the impression that the Federal Government should become a heavy-handed regulator and fix prices whenever it is politically expedient.

This hearing is an opportunity to explore all these issues in more specific detail, including the effectiveness of the administration's so called exchange program, and whether the program will have any significant economic impact on crude oil supplies in home heating oil prices. I look forward to hearing the testimony of the witnesses.

I will be happy to recognize the distinguished ranking member, the gentleman from Virginia, Mr. Boucher, for an opening statement.

Mr. BOUCHER. Thank you very much, Mr. Chairman.

I will take the opportunity of these remarks this morning to express my disappointment at the tone and tenor that surrounds this proceeding. As the members know, I hold strong belief in the benefits of bi-partisanship and I rarely criticize the processes of this committee. But I see this hearing as nothing more than a blatantly partisan attempt to deride the administration for its recent efforts to help the American people through what is expected to be a long and cold winter.

Further, Mr. Chairman, I am disappointed that after the last hearing on this precise subject matter the chairman of the full committee and the chairman of the subcommittee sent letters to the Department of Energy posing questions regarding both the exchange of oil from the SPR and the bidding process that DOE uti-

lized to facilitate that exchange. Mr. Dingell and I were technically copied on these letters but, nonetheless, did not receive those copies until the minority staff learned of the existence of those letters and requested that the copies be sent. Those letters clearly signaled the intent of the majority to pursue this matter further, and some advance notice of that intention would have been much appreciated.

Mr. Chairman, I understand that today we will once again be discussing the legal authority of the DOE to conduct the SPR exchange. We will be addressing the bidding process and the exchange's potential effect on heating oil supplies and prices. While I understand your frustration and your disagreement with the administration regarding the use of the SPR in this matter, I would point out this is the third time the members of this subcommittee have been asked to delve into the authority of the DOE to conduct this exchange. This is a matter about which lawyers differ and this subcommittee, no matter how many hearings on the subject we hold, is unlikely to resolve.

If the majority believes that the DOE bidding process deserves further scrutiny, that task could be pursued more effectively if there had been time for members to digest the information DOE provided in response to the chairman's letters. In fact, this inquiry could be best pursued after the completion of the bidding process when the results of the process were more in evidence.

Despite my disappointment with today's hearing, I am much more greatly concerned that this Congress has not taken sufficient action to address the potential energy problems for consumers this winter. While here in the House we did work together on a bipartisan basis to reauthorize the Energy Policy and Conservation Act, and I want to thank the chairman for his leadership and excellent work with our side in advancing that measure in the House, the passage of the bill is now stalled in the Senate; and congressional leadership has, in my view, failed in its responsibility to reauthorize this expired legislation which is the foundation of our energy emergency preparedness.

Further, Congress has underfunded the very successful Low Income Home Energy Assistance Program and the weatherization assistance programs which are vital to assisting low income families and senior citizens across the country in paying for high heating and cooling bills. Congress has also reduced funding for Federal energy conservation programs and energy conservation R&D programs by significant amounts.

American consumers this year are faced with paying an extra \$50 billion in the form of higher gasoline and home heating oil prices. Serious questions remain about the adequacy of home heating oil supplies for this coming winter in some regions of the Nation.

Regardless of whether we fully agree with the actions that the administration has taken, the administration has at least taken steps to ward off potential energy supply and pricing problems, from releasing energy funds for LIHEAP, to establishing the Northeast Petroleum Reserve and finally conducting the exchange from the SPR. This Congress, on the other hand, has in my view failed in its responsibilities to America's energy consumers.

Mr. Chairman, we have enjoyed and continue to enjoy a good relationship; and I value the bi-partisan approach which has been your hallmark in your leadership of this committee. I congratulate you for that and for what I think has been some really excellent work that you have undertaken during the past 2 years. I am certain that, this unfortunate episode notwithstanding, our productive work together to advance sound energy policies will continue.

I thank you, and I yield back.

Mr. BARTON. I want to thank the distinguished ranking member, and I want to apologize for myself. It was not my intent to mislead or to keep in the dark the minority on that letter. We announced it at the hearing. If for some reason the staffs did not get a copy, that is my responsibility, and I take full responsibility, and I am willing to apologize in writing if that helps the effort. Sometimes we do have to disagree, but we can always disagree agreeably, and it has been a pleasure to work with you and the other members on the minority on this subcommittee this year. And sometimes we understand that there are going to be differences that have to be aired, but I do apologize for any non-inclusion of the effort to gather the material for this hearing and this issue.

I would recognize the gentleman from Illinois, Mr. Shimkus, for an opening statement.

Mr. SHIMKUS. Thank you, Mr. Chairman, and for everyone who showed up today and also our colleagues who will testify in hopefully not too long of a time.

No one should be surprised at Chairman Barton's dogged oversight over the SPR. As a member of 4 years, I don't know of one issue that Chairman Barton has not taken—even when we had low energy the SPR has been something that Chairman Barton has been doggedly in pursuit of the truth. So I want to applaud the chairman for his consistency.

For the past several months I would say that our country has been on the verge of an energy crisis. Oil and natural gas prices have skyrocketed to almost record highs. The price increase now poses a threat to our country's continued economic growth, and we continue to ask the question what can be done.

We have heard from this administration the constant course of the blame game. They blame it on big oil. They blame it on corporate America for gouging American consumers. They blame it on the Republican-controlled Congress for not passing their energy agenda. They will blame anybody and everybody, as long as it isn't them.

Their solution is to release 30 million barrels from our oil strategic oil reserves. As a former Army officer and current Army reservist concerned with the national defense, I think about the Strategic Petroleum Reserve, and I highlight the word strategic. It is a strategic reserve to be used in times of a national emergency. It isn't our strategic political reserve to be used in times of political pressure.

What happens now if the problems in the Middle East continue to grow? What are we going to use to fuel our tanks, to fuel our jets? That oil is there for our national security. We now have 30 million barrels less oil to meet a possible national emergency.

So when I see what I think is a use of the SPR to fix prices, I see it as an assault on our men and women in uniform whose lives may be dependent on our Strategic Petroleum Reserve being used to fuel our weapons of war should we need it, and that is my focus as still being involved with the defense forces of our Nation. The SPR was established to protect Americans from a cutoff of oil imports, not to manipulate prices and not for political gain.

While it may be well-intentioned to move to swap some reserves, this will do little to address our Nation's heavy dependence on foreign oil and most likely will not impact price. And the way was swap was handled was laughable. Seven million barrels of oil had to be reauctioned because the companies DOE gave the oil to did not even have the money to purchase the oil.

When I used to be a county treasurer and I had tax auctions, we would at least ask for a letter of credit. This was not done, and no research on the bidders occurred. Instead of giving this oil to actual oil companies or refiners, DOE gave it to groups like Dean Witter, whose sole intention was to make money. To top it off, there was no guarantee that the oil was even going to go to the Northeast where it was needed most. Reports in the press said companies were using the oil from the SPR to replenish oil that they were sending to Europe where heating oil is even more expensive.

With regard to home heating oil, I would like to mention one thing that may help the supply problem, and it wouldn't come to anyone on this committee's surprise, and that is biodiesel. Since biodiesel is made domestically with renewable resources, using it at blended levels with home heating oil would still produce dependence on foreign oil and increase our supply.

My colleague to the left asked if that was made from corn. It is really a product of soybeans and beef tallow and some other products we have in plentiful supply in this country and especially in Illinois and especially in the 20th district of Illinois. While there may be some concerns with using biodiesel as home heating oil, there should be no problems when blended at low levels between 5 and 20 percent. Even at those small levels it should stretch supplies enough to last the winter and keep the prices at reasonable levels.

Although we are currently talking about biodiesel use in the home heating oil market this year because of the high price of heating oil, to help avoid the situation in the future we should be developing a long-term strategy for integrating biodiesel and other alternatives into home heating oil every year. Biodiesel can help displace imported petroleum, improve air quality and support domestic industries like agriculture; and I have a lot of agriculture in my district. I happen to think that our Nation should not rely only on just one energy source such as natural gas, coal, oil, nuclear, hydro, solar and wind to generate power, but all these sources. It is the smart thing to do over the long haul. Just like any good retirement portfolio, our energy industry should be diversified.

Again, Mr. Chairman, thank you for having this hearing. I do think it is going to be beneficial.

I yield back the balance of my time.

Mr. BARTON. We thank the gentleman from Illinois.

I recognize the gentleman from Maryland, Mr. Wynn, for an opening statement.

Mr. WYNN. Thank you very much, Mr. Chairman.

First, I would like to commend the leadership and efforts of the Secretary, Bill Richardson, and the staff of the United States Department of Energy, particularly the Strategic Petroleum Reserve Office, in their effort to make sure that the oil from the SPR reaches the marketplace in an efficient manner. I think this addresses very legitimate and real concerns about high home heating oil prices during a potentially long and cold winter, and it is a more than adequate substitute for extensive rhetoric that seems to occur around this place.

I understand that the SPR offered 11 contract awards, and only two companies were unable to meet the letter of credit requirement imposed by the SPR oil exchange process. This represents in my view an over 80 percent rate of success on the first solicitation. According to the SPR office in Louisiana, it is not unusual to solicit more than one round of bids or to receive bids for less than the amount of oil that is offered for solicitation.

As a member of the committee, I was pleased to note that three of the initial contract recipients were small minority businesses. This is a testament to the continued sophistication of small businesses and the changing environment of the energy industry.

The fact is that trains of all sizes can get oil to the marketplace in a very efficient manner. Increased access to the energy industry for small businesses is a natural development given the increased sophistication of America's small business community, which incidentally provides more than 50 percent of the private work force and is a principal source of new jobs in this country.

At this point, I would like to raise my concern about the highly unusual and I would consider highly unfair scrutiny that the U.S. Department of Energy and several small minority-owned businesses have received during the solicitation and contract award process and also by this committee, quite frankly. The assumption made by members of the press and perpetuated by officials of big oil do not serve the best interest of our country.

Let me begin right up front. An editorial ran in the Wall Street Journal October 11. The editorial began by making light of the fact that 3 of the 11 companies the Department of Energy entered into the swap agreements with were small businesses that have little experience in the oil business, according to the Journal, but among the winners were three tiny oil companies nobody in the oil industry had ever heard of. The fact of the matter is, the Wall Street Journal doesn't stop there, claiming that the only reason such small businesses could qualify would be because of special treatment or that they put forward a shady front.

The Journal continues, perhaps these three have very good friends in the Energy Department. Perhaps big oil has good friends in the Energy Department as well. Perhaps they are just a front for low-down types. Perhaps big oil has been gouging the American consumer. Perhaps they are just shells to prop up prices when it looked as though the auction might not command a lot of interest.

My point is this is unfair speculation, ungrounded speculation; and no evidence was ever presented to support these contentions.

This country's economy was founded upon entrepreneurs who recognized opportunity and competed against tough odds. That is what happened in this case. The sarcastic and disrespectful tone taken by the Wall Street Journal officials for big oil concerning the legitimacy and qualifications of these small businesses is a great disservice to this country, and I am sad to say they may have jeopardized the chance of these small business from securing their letter of credit. In fact, only one of these companies actually was awarded a contract, despite all three making qualified bids.

The truth is that these three small businesses had every right to compete for this oil and to compete for these contracts, regardless of their size. They had every right to win the contract if they provided proof of financial credit.

The Department's solicitation developed by career staff was designed to meet two goals. One to get oil from the SPR into the marketplace as quickly as possible and, two, to ensure that the government and the taxpayer receive adequate protection.

Let me emphasize that there was no size restrictions in the solicitation, and there should not have been. The truth is that the solicitation did not require bidders to offer bundled services of transportation, refining or trading. That is not necessary, and it is not required, and it should not be required. Today the energy marketplace is largely unbundled. A trader can often get oil to the marketplace in the quickest and most efficient manner.

The goal of the solicitation was to encourage as many bidders as possible, both small and large companies, so the oil could be moved to the market quickly. In fact, the oil that was exchanged in the first round has already started reaching the marketplace, including the oil of the participating small businesses. The truth is that the government and taxpayer were fully protected against the loss of value of any oil in the Reserve, no matter how large or small the bidding company.

The solicitation required all bidders to provide a letter of credit from a certified financial institution for the full value of the crude oil. If proof of credit was not received, no oil would be delivered. That is exactly what happened. The Department recently announced that 23 million barrels of oil is on its way to the market, the largest sale of swap conducted in the SPR's 25 year history. The same amount or more oil would be returned to the SPR by the winning contractors next year.

Mr. BARTON. Would the gentleman from Maryland yield briefly?

Mr. WYNN. I would be happy to.

Mr. BARTON. I will let the gentleman continue because I think what you say is relevant to the hearing, but, theoretically, opening statements except for the Chair and the ranking member are 3 minutes. And you are in the tradition of Ed Markey, going on with about a 10-minute opening statement. Since we don't have that many attendees and you are so eloquent, I am very willing to listen to it, but just to remind that you might begin to wrap up here in the next minute or so.

Mr. WYNN. Thank you, Mr. Chairman; and I will be wrapped up very shortly.

Let me say, in terms of our bottom line, a grave injustice has been done to these small businesses; and I feel very bad about this.

I believe attention should be given to the role the large producers played in adversely affecting the commitments made to these small businesses by their initial partners.

In light of the chairman's comments—and he has been very generous—I would conclude my statements by indicating a willingness to continue to work on this issue and look at ways in which we can effectively include the small business community in contracts such as these.

Mr. Chairman, I thank you for your generosity.

Mr. BARTON. I thank the gentleman from Maryland.

The gentleman from North Carolina, Mr. Burr, is recognized for an opening statement.

Mr. BURR. I thank the chairman.

The gentleman from—Mr. Wynn is 100 percent correct. We have had unfair criticism, unfair criticism of the companies that bid, unfair criticism from the Department of Energy. Because every member of this subcommittee should know that, from our past experience on contracts, that the Department of Energy is incapable of carrying them out. They are incapable of designing them correctly. They are incapable of executing them. And for us to look at just another blunder in the contract process that they were warned of in a meeting open to all members of this committee—and I believe that the chairman and myself were the only ones there when we sat down with them and said, how can we be assured that this product ends up in the United States? And they said, we can't. A flawed process.

But I also want to address some of the statements my good friend Mr. Boucher said. This is not something new that this committee has just taken on. We signed a letter earlier this year in the year 2000 raising questions with the Department of Energy about the spike last year in fuel oil prices.

I will read you comments of Mr. Mazur, Office of Policy. He is the director. I take for granted from that title he is important.

But in his response he said this to Chairman Bliley: While some have argued for release of oil from the SPR there as a way to bring down world oil prices, we do not believe that a release at this time would be desirable. The SPR is intended for release only in the event of a major oil supply disruption, not for trying to manage the world market of nearly 74 million barrels a day of oil.

I think they made it very clear then they were against it. This was not even a consideration. This was on the heels of high prices and shortages in New England, much like we face today.

I go on and speed up the clock to later this year, the decision by the President, the announcement to sell SPR; and I go immediately to a memorandum to the President from Larry Summers, Secretary of the Treasury. He starts off: Chairman Greenspan and I believe that using the Strategic Petroleum Reserve at this time, as proposed by the Department of Energy, would be a major and substantial policy mistake. Even DOE suggests its impact on heating oil prices would be quite small. Moreover, it would set a new and ill-advised precedent, and the claim, the exchange is nothing more than a policy of technical SPR management, would simply not be credible in the current environment.

They went on to describe several points that they wanted to make to the President. Let me share one of them with you.

Using the SPR at this time would be seen as a radical departure from past practice and an attempt to manipulate prices, the one thing DOE said they would not do.

It goes on to say, given the substantial size of the proposed sale and its proximity to both the OPEC meeting and the November election, it will be impossible to argue credibly that the proposed exchange is simply a technical SPR management policy.

The only reason that this question arises is because 4 years ago in 1996 we had an SPR sale. We sold 12 million barrels. The statement by the President at the time said: Over the last several weeks I have been concerned about the rise in gasoline prices at the pump. Today I am directing the administration to take the following steps: First, I am asking the Secretary of Energy to immediately begin the process of orderly sales of approximately 12 million barrels.

In 1996, it was because of high gasoline prices. Earlier this year, they wouldn't consider it because prices aren't a part of the decision to sell SPR.

Mr. Chairman, the Secretary of the Treasury said, Mr. President, this is the wrong thing to do. Mr. Wynn is right. We are unfairly criticizing this process because we know they are incapable of carrying it out.

Mr. Chairman, I appreciate you holding this hearing. I wish that it would do some good. But the reality is that the flawed process of the companies that could participate in putting more oil into the system may or may not be part of this bidding process. But there is one thing that I hope we can agree on, both sides of the aisle on, and that is that we have to have a design process with a very specific set of goals as it relates to the use of SPR, the size of SPR and the process that we go through when there is any type of sale like we have currently going on, not one where we argue and debate the code of law that they have chosen to use and certainly so there is not a misunderstanding from administration to administration about what its use is for.

I kindly yield back to the chairman.

Mr. BARTON. I thank the gentleman from North Carolina.

I would recognize the gentleman from Florida, the vice chairman of the subcommittee, for an opening statement.

Mr. STEARNS. Thank you, Mr. Chairman; and thank you for holding this hearing.

I want to be the one to be in the same camp as others who say it is very important that you hold this hearing, particularly in light of the fact that DOE claimed that in the interest of time it decided not to prequalify bids for the oil; and of course, as a result, two of the awarded bids were retracted because the companies could not obtain the necessary letter of credit. And now DOE has had to initiate another solicitation for the remaining oil.

Mr. Chairman, I remain unconvinced that the release of the Reserve is imperative. First of all, the Department of Energy has indicated that only one-third of the 30 million barrels would even reach U.S. Refineries.

I am also concerned that much of the remaining 20 million may not even remain in the United States' market. Questions have been raised as to the refineries' ability to handle the additional oil, as most are operating near capacity; and, furthermore, one of the witnesses before us today indicated in his testimony that the primary terminal in Netherland, Texas, will be unable to handle the release of SPR oil for November, thereby delaying delivery well into December. It seems that the administration decided to go ahead and release the oil and then figure out the details as it went along.

I think this is part of the whole program that has come out of the Department of Energy. I think this speaks to the general lack of leadership which many of us talked about earlier. Instead of tackling our energy problems head on with a coherent policy, the administration chooses to run in a circle, throwing money at the problem or proposing politically expedient policies which fail to address a long-term solution.

Mr. Chairman, I think one of things which certainly could be helped is to take under the Jones Act and use a waiver so that we could move heating oil or crude oil from the Gulf Coast to the Northeast; and I want to hear from the panel about perhaps a Jones Act waiver that could make it, could help, sort of the oil needed in New England.

And last, Mr. Chairman, if the administration is indeed looking to provide heating assistance to America, where is the help for those homes that use natural gas? I doubt that the release of \$400 million in LIHEAP funds will provide enough help with natural gas prices for all Americans.

Thank you, Mr. Chairman.

Mr. BARTON. Thank the gentleman from Florida.

The gentleman from Oklahoma would be recognized for an opening statement.

Mr. LARGENT. Thank you, Mr. Chairman, for holding this hearing. It is a very timely one. As the 106th Congress draws to a close, I believe this subcommittee should exert its jurisdictional responsibility to closely examine the administration's decision to draw down the Strategic Petroleum Reserve.

When this subcommittee held a hearing a few weeks ago on the President's decision to release 30 million barrels in the form of a swap from the SPR, I was extremely skeptical about the timing of the release. At that time I stated that I thought the release of the SPR made for a good election year campaign tactic, but as a public policy matter it was a bad idea.

After reading some of the news reports of virtual novices in the oil business viewing the release of SPR as a quick get-rich scheme, as well as oil industry analysts who had publicly stated that the reason the government failed to receive more generous bids suggests that refiners are not having trouble finding crude oil in the market, that makes me even more skeptical about the validity of releasing 30 million barrels from the Strategic Petroleum Reserve.

I think our colleague, Mr. Shimkus, was right on target at the previous hearing when he stated that the operative word in Strategic Petroleum Reserve is "strategic". I am concerned that this administration, based upon what happened with the bidding process, confused the word "strategic" with "speculative". If DOE has a rea-

sonable explanation why it suspended its usual requirement that each bidder supply financial guarantees, I would like to hear it.

Mr. Chairman, the United States' ability to maintain some form of energy independence is one of our highest national security priorities. Recently, we have seen tensions rise in the Middle East. Tragically, 17 brave Americans lost their lives aboard the USS Cole last week in Yemen. Let me be clear, I don't believe there is any correlation whatsoever between the release of SPR and the bombing of the USS Cole. However, I do believe there is a very real correlation between our national security and our reliance on foreign sources for crude oil.

I recommend every member of this subcommittee as well as every Member of Congress take a look at a chart compiled by the Congressional Research Service that shows that 7.8 percent of the crude oil received by the SPR since 1995 is supplied by Libya, Iran and Iraq. How much has the U.S. Domestic production supplied over that same period? Exactly that same amount, 7.8 percent to the Strategic Petroleum Reserve produced by the United States. That should serve as a wake-up call to all of us, regardless of whether we represent an oil-producing State or not.

Mr. Chairman, I look forward to hearing from our witnesses, particularly Admiral Watkins. I believe Admiral Watkins, as a former Secretary of Energy and highly accomplished naval officer, can offer an insightful perspective on the national security implications of drawing down the Strategic Petroleum Reserve when there has been no discernible disruption in our energy supply.

I yield back my time.

Mr. BARTON. I thank the gentleman from Oklahoma.

I would recognize the distinguished gentleman from Louisiana, Mr. Tauzin, for an opening statement.

Mr. TAUZIN. I thank you, Mr. Chairman, and thank you for allowing me to join the hearing today.

Let me first address the concerns raised by our friend from Virginia about this hearing. I am, frankly, sorry that he has some suspicions that this is political in nature. It certainly should not be. This committee of Congress has primary jurisdiction over the SPR. The SPR is not an administration reserve. It is a national reserve. And this committee's obligation is to see whether or not it is being operated for the good of the Nation or whether it is being used as some sort of political tool.

There are suspicions about that, I would add. There are serious suspicions about the decision to release 30 million barrels right before this election, particularly when the last release was in 1996, another election year.

The seriousness of the concern is summarized by Larry Summers himself and Greenspan to the President saying, don't politicize this reserve. It is not in the Nation's interest. It is not in the Nation's interest because, No. 1, releasing as much as 60 million barrels would do no more good than perhaps the 2.3 cent change in the price of fuel oil, a minimal impact. Thirty million barrels would obviously have a smaller, perhaps as little as one cent, impact. In fact, experts say that only 10 million of these barrels will actually be used in the process of making fuel oil. The other 20 will replace

oil that would have been imported into the U.S., and of that 10 million it might produce as little as 250,000 barrels of fuel oil.

One of the reasons we have a problem is that our refineries are at 94 percent capacity. We have not built a new refinery in America in 20 years, and in the last dozen or so years over 30 refineries have shut down in this country. So we have a problem with refining the crude oil that is brought into this country from places like Iran and Iraq, much less turning it into fuel oil for folks who will need it.

We also have a memorandum from John Shans, sent to Melanie Kenderdine, the Director of Office of Policy, noting that all that was sold to Morgan Stanley is probably going to get exported. Because Morgan Stanley in their memo says that the Colonial pipeline is so full they can't move it up north. They have got fuel all in abundance in the Gulf Coast. They can't move it up north because the pipelines are full. In fact, they will probably export that fuel oil to Europe.

What is amazing is that the DOE, in preparing the contracts to handle this 30 million barrel release that Larry Summers and Greenspan indicates looks too political and it is a bad policy decision, it is a decision to take the national strategic reserve and turn it into something used in political campaign years. That, they think, is wrong. In fact, they say at the end of their summary, Mr. President, you are taking responsibility for the prices of energy when you start doing this. Do you really want to do that? Do you want to be responsible for high prices of energy? Because once you take control of the SPR and release it to control prices in the marketplace, then you assume responsibility for those prices. Do you really want to do that?

That is what Larry Summers wrote. But even considering all of those political questions about the use of the SPR, to administer these contracts as horribly ineptly as DOE and the Department has apparently done now just adds insult to injury. These contracts—I don't know if you read the stories on them—even permit the sale of this oil overseas. It allows these bidders to take this oil in with no cash, by the way. And the Wall Street Journal is interesting, Mr. Wynn. It says, who would not want to own 10 million barrels of oil with no money down and 12 months to pay? What a neat deal.

Mr. WYNN. Will the gentleman yield?

Mr. TAUZIN. I will yield in a second.

Not only did it allow these contracts to go to people with no experience in this business, with no money down, 12 months to pay, but it even included language that allowed them to export it overseas. Why would the DOE construct a contract that is specifically designed to take oil out of our strategic reserve for the stated reason of getting fuel oil to the Northeast and leave in the contract a provision that says it is okay to sell this oil to Europe once you have produced it into refined fuel oil for homes? What a stupid provision. This is ineptness. This is ineptitude at its worse. So, yes, there is a lot of suspicion about what is going on with the SPR.

Mr. WYNN. Will the gentleman yield?

Mr. TAUZIN. If I have time I will yield to my friend.

Mr. WYNN. I thank the gentleman for yielding. I just wanted to clarify one point, because I think these companies are being unfairly indicted. I indicated at the end of my statement I am willing look at ways we can improve this process, but the fact of the matter is that every company that received oil would have to have proof of credit. If no proof of credit is received, no oil would be delivered; and that is exactly what happened. So any suggestion that anybody got oil without paying for it or had a year to go until they paid is not accurate. The truth of the matter is, proof of financial ability. It had to be provided. Credit had to be in hand before the oil was received—

Mr. TAUZIN. My point is—

Mr. BARTON. The opening statements are for opening statements. Opening statements are not to have a debate about the hearing.

Mr. TAUZIN. Well, let me conclude, Mr. Chairman, if I can. I simply want to point out that the DOE has not only used the SPR release for political purposes in my opinion, in many people's opinion, but it has used it now for social policy to award contracts to people with no experience in this business before—

Mr. WYNN. Will the gentleman yield?

Mr. TAUZIN. No, I will not. That is social policy. That is what it is. Instead of making sure that people are capable and they have done this before so oil can get to where it belongs, they have awarded it to people with no experience. That is social policy.

Mr. BARTON. Will the gentleman conclude his opening statement?

Mr. TAUZIN. I will conclude.

Finally, it will have such a small impact on the availability and the prices of fuel oil in the Northeast that it is a shame we are going through this exercise.

I yield back.

[Additional statements submitted for the record follow:]

PREPARED STATEMENT OF HON. JOHN SHADEGG, A REPRESENTATIVE IN CONGRESS
FROM THE STATE OF ARIZONA

Three weeks ago, at our September 28 hearing, we examined the high price of heating oil and the Administration's decision to release oil from the Strategic Petroleum Reserve (SPR). Today, we have the opportunity to conduct further oversight into the utter failure of the Administration's decision. This decision is a perfect example of a fact which we all should have learned when the Soviet Union fell a decade ago: interference by the federal government in the economy does not work.

The record speaks for itself. On September 20, 2000, crude oil sold at \$37.21 per barrel. On September 22, the Administration announced the release of 30 million barrels of oil from the SPR for the stated purpose of lowering the price of heating oil this winter. The market reacted to the news by dipping to \$31.57 per barrel on September 25. Yesterday, less than three weeks after the announcement, the price of crude oil was back up to \$33.48 per barrel. So much for the Administration's plan to lower heating oil prices this winter.

Could the federal government have a positive impact on the price of heating oil? The answer is yes: by minimizing the burdens it places on the economy. For example, approximately 28 percent of the price of refined petroleum products is attributable to taxes. It does not take a Nobel Prize in economics to understand that if you reduce or eliminate 28 percent of the cost of a product, you will get a significantly lower end price.

The Administration could even take a step which would have a very positive long-term effect on oil prices: it could end its prohibition on oil exploration and production in the Arctic National Wildlife Refuge (ANWR) on the North Slope of Alaska. There is an estimated supply of at least 3.57 billion barrels of oil underlying a portion of ANWR. Private industry has the technology to extract the oil with very little degradation of the environment.

Much of the recent price rise is directly attributable to the violence in the Middle East and the fact that the United States depends on imports for 62 percent of its oil supply. Again, it does not take a Nobel Prize winner to realize that Minimizing our exposure in a volatile area of the world through development of greater domestic oil production will bring a measure of stability to prices.

The federal government is not a business. Moreover, when it attempts to act like a business, any positive result is liable to be as short-lived as those following the Administration's announcement of the SPR release. When the government steps aside, minimizes its burdens on the private sector, and allows the economy to take care of itself, the results are the long-term growth and economic efficiency that only private enterprise can deliver. I hope that this and future administrations can learn from this important lesson.

PREPARED STATEMENT OF HON. TOM BLILEY, CHAIRMAN, COMMITTEE ON COMMERCE

Mr. Chairman: I'd like to commend you for holding this hearing on the Department of Energy's Drawdown of the Strategic Petroleum Reserve. Over the past year, energy issues have been very much in the news. The Committee on Commerce takes very seriously rising prices for crude oil, heating oil, gasoline, and natural gas. Members of this Committee wish to prevent a home heating oil crisis this winter. When DOE announced the release of 30 million barrels of oil from the Reserve, this Committee was especially interested in the impact this would have for consumers.

One thing is for sure. This unprecedented action so close in time to the Presidential election is troubling.

I have always been of the view that Congress and the Administration need to be working together on energy policies. Our objective is to look out for consumers, to reduce the nation's dependence on foreign oil, and to increase our energy independence. We need to craft environmentally sound policies that will stimulate, not hinder our energy security.

The petroleum reserve is a valuable strategic asset that belongs to the American people. The Reserve was built and filled to protect against severe energy supply disruption. Most importantly, we should not engage in short-term election year gimmickery with the Reserve. If this is the case, it is wrong to trifle with the Reserve in this manner.

I believe it is important to look at the Release or Exchange of 30 million barrels of oil. This Administration claims that they released the oil to help consumers make it through the winter. Will this program actually help consumers who use home heating oil? Or will home heating oil made from oil released from the Reserve be exported outside of the United States?

I am also concerned about how DOE is administering the contracts for oil and whether the American public is getting value for this use of the Reserve.

Today I hope to learn the answers to these and many other questions. I look forward to hearing from today's distinguished panel of witnesses. Thank you.

Mr. BARTON. All right. With those mild-mannered, non-controversial opening statements, we are now ready to hear from our panel of distinguished Congressmen and Congresswomen, if Congresswoman Cubin would take her place at the witness table. We will start with Congressman Hinojosa, who is the first member present; and we will go to Congresswoman DeLauro, who is the second member present; and then to Congressman Knollenberg and then Congresswoman Cubin.

Congressman Hinojosa, welcome to the subcommittee. It is good to have another Texan here. Sometimes I feel outnumbered, so I am glad that you are here. Your statement is in the record in its entirety. We will recognize you for 5 minutes to summarize it.

**STATEMENT OF HON. RUBÉN HINOJOSA, A REPRESENTATIVE
IN CONGRESS FROM THE STATE OF TEXAS**

Mr. HINOJOSA. Thank you Mr. Chairman. I appreciate that you would allow me to submit all my testimony in writing and that I can just summarize it and possibly do a correlation to this and the experience that I bring before coming to Congress—

Mr. BARTON. Without objection.

Mr. HINOJOSA. [continuing] and where I make my living.

Mr. Chairman, I appreciate the opportunity to testify today. I will make brief remarks, and I will also submit my testimony for the record as you approved earlier.

I would like to commend the leadership and the efforts of Energy Secretary Bill Richardson as well as the entire staff of the U.S. Department of Energy, particularly the Strategic Petroleum Reserve, that I will refer to as SPR, in their effort to ensure that oil from the SPR petroleum reserve reaches the marketplaces in an efficient manner.

I know that this subcommittee will be monitoring the larger issues regarding the oil exchange. However, I choose to focus my remarks on the participation of the small and medium minority businesses in this solicitation. As part of what I am submitting to the record, I have a letter dated September 28, 2000, addressed to the Honorable Bill Richardson, Secretary of Energy, and in that letter which I signed, and I will only read a part of it, I said, "I participated in last night's Minority Enterprise Development Week Conference gala dinner, and I was happy to hear that you entered into a memorandum of understanding with the United States Department of Commerce's Minority Business Development Agency and the National Minority Business Summit to increase business activity between the Department of Energy and minority-owned firms. As a member of the House Small Business Committee, I am a strong supporter of programs that increase the participation of minority-owned companies in Federal procurement and activity, and I believe that the inclusion of minority businesses is important to the economic vitality of the Nation."

It is this letter that makes me a participant of this hearing today.

I know that this committee will be monitoring the large issues, as I said earlier, but I want to say that as a member of the House Small Business Committee, I was happy to hear that three of the initial contract recipients were small minority businesses.

Increased access to the energy industry for small and medium businesses is a natural development, given the increased sophistication of America's small business community. Today America's 25 million small businesses employ more than 50 percent of the private work force and are the principal source of new jobs in America.

Without going into all of my prepared text, Mr. Chairman, I want to say that yesterday I attended the ceremony to honor the 17 dead and missing sailors on the USS Cole in Norfolk, Virginia, a very, very sad occasion for our country, especially for the families of those sailors we lost in the Middle East. As I was driving, as I was actually riding in a bus with about 25 Senators and 25 Congressmen to this place in Norfolk, it reminded me of something that happened that I want to relate to the members of this committee.

Before coming to Congress, I served as president of a food processing company for 20 years, a company that was very small, had less than half a million dollars in annual sales, and I, as president, applied for the 8-A designation, and with lots and lots of difficul-

ties, I finally got that designation and found it very difficult to get into the Federal procurement industry, into the Federal procurement program here in Washington. However, with my persistence and lots of hard work, I got there.

So listening to what I heard in the opening remarks and how you have to have all of this experience in order to get into the oil business reminds me of what I heard as to not having the experience to be able to supply meat to the Department of Defense back in the 1980's. But in 1990, as president of the company, I received a request from DPSC, Department of Personnel Support Centers, in Philadelphia, saying that they needed 1 million pounds of ground meat to be loaded onto one of our warships headed to the Middle East and had to be delivered within 72 hours to the lowest bidders. So I responded by saying that I needed just a few hours to give them a response in writing.

I closed down the plant, and I called all of the employees, all of the supervisors, and I told them the situation that we were finding ourselves in as we went into war. Our men had to eat, they needed food on that warship. I asked if they were willing to work around the clock and in 72 hours be able to meet that deadline. Yes, they did. They stood up to the challenge and 2 hours to spare. In 70 hours, we were able to deliver—not 1 million pounds, but a half a million pounds in a convoy of 14 trailerloads of ground meat.

I say this, Mr. Chairman, because we were told that only ConAgra and Excel and those large companies could do this, but I am saying to you that small businesses are asking for an opportunity to be able to get into this Federal procurement program, and, when put to the test, we can do lots of things that big boys think we can't do.

Do we still have time to continue?

Mr. BARTON. You have gone about a minute and a half over. If you would wrap up in the next 30 seconds.

Mr. HINOJOSA. Fine. I want to simply summarize and say that I have included that editorial that Congressman Wynn talked about in the Wall Street Journal, which is probably one that I think should not have been written in the way that it was, because it is detrimental to small businesses like ourselves, and that there are many in my committee, including our Chairman Jim Talent and our Ranking Member Nydia Velazquez, who are fighting, who are fighting for these kinds of opportunities as these three would have been given had we not had this article in the Wall Street Journal, which, in my opinion, probably caused two of them to not be able to get their letter of credit and be able to get into this Federal procurement. Be a little bit more mindful of those small and medium businesses who are creating the jobs that are making our economy so strong and an unemployment rate of 3.9 percent. Thank you, Mr. Chairman.

[The prepared statement of Hon. Rubén Hinojosa follows:]

PREPARED STATEMENT OF RUBÉN HINOJOSA, A REPRESENTATIVE IN CONGRESS FROM
THE STATE OF TEXAS

Mr. Chairman, I appreciate the opportunity to testify today. I will make brief remarks and I will also submit my testimony for the record. I also would like permission to extend and revise my remarks.

I would like to commend the leadership and the efforts of Energy Secretary Bill Richardson as well as the entire staff of the U.S. Department of Energy, particularly the Strategic Petroleum Reserve (SPR) Office, in their effort to ensure that oil from the SPR Petroleum Reserve reaches the marketplace in an efficient manner.

I know that this subcommittee will be monitoring the larger issues regarding this oil exchange; However, I choose to focus my remarks on the participation of small and medium minority business in this solicitation.

As a member of the House Small Business Committee, I was happy to hear that three (3) of the initial contract recipients were small minority businesses. Increased access to the energy industry for small and medium businesses is a natural development given the increased sophistication of America's small business community. Today, America's 25 million small businesses employ more than 50 percent of the private workforce, and are the principal source of new jobs in America.

However, I want to take this opportunity to raise serious concerns I have about the highly unusual, and I would argue highly unfair, scrutiny the U.S. Department of Energy and several small or minority owned businesses have come under during the solicitation and contract award process for the exchange of oil from the SPR. The assumptions made by many of the members of the press and perpetuated by officials from large oil interests are alarming.

Let me start up-front with an editorial entitled "Bidding on the Reserve" that ran in *The Wall Street Journal* October 11th, and which, with your permission, I will insert into the hearing record. This editorial begins by making light of the fact that three of the eleven companies the Department of Energy (Department) entered into swap agreements with are small businesses and have little experience in the oil business. Quoting the Journal: **"But among the winners were three tiny oil companies...nobody in the oil industry has ever heard of them, none of them seem to have refining capacity..."** *The Wall Street Journal* does not stop there, claiming the only way such a small business could qualify would be because of special treatment or that they put forward a shady front. Quoting the Journal: **"Perhaps these three have a Very Good Friend in the Energy Department? Perhaps they are fronts for some low-down types? Perhaps they are just shells to prop up the prices when it looked as though the auction might not command a lot of interest from the standard suspects?"**

Mr. Chairman, this country's economy was founded by entrepreneurs who recognized opportunity and competed against tough odds. These three companies recognized an opportunity and competed fairly according to the rules set out by the Department. The sarcastic and disrespectful tone taken by the Wall Street Journal and officials from large oil interests concerning the legitimacy and qualifications of these three small businesses is a great disservice to the country. And, I am sad to say, that may have jeopardized their chances for securing their letters of credit. In fact, only one of these three companies was actually awarded a contract despite the fact that all three submitted qualified bids.

Today's energy marketplace is largely unbundled. A trader can often get oil to the marketplace in the quickest and most efficient manner. The goal of the solicitation was to encourage as many bidders as possible, **both** small and large companies, so that oil could be moved into the market quickly. In fact, the oil that was exchanged in the first round has already started reaching the marketplace, including the oil of the participating small business.

The truth is that these three small businesses had every right to bid for the oil contracts regardless of their size and experience because they met all standards as set by the Department. There was no processing or refining standard because it is not necessary in this instance. The oil is only being traded. They had every right to win a contract if they offered competitive bids and provided proof of financial credit. The Department's solicitation, developed by career staff, was designed to meet two goals: 1) to get oil from the SPR into the market as quickly as possible, and 2) to insure that the government and the taxpayer received adequate protection against the value of the SPR oil. There were no business size restrictions in the solicitation.

The fact is that the government and the taxpayer were fully protected against the loss of value of any oil in the reserve, no matter how small or large the bidding company. If proof of credit was not received, no oil would be delivered. In fact, the government and the taxpayer will benefit from the exchange. The Department recently announced that 23 million barrels of oil are on their way to the market, the largest sale or swap conducted in the SPR's 25 year history. The same amount of, or more, oil will be returned to the SPR by the winning contractors next year.

In summary, the three small businesses who bid for the oil exchange contracts met all qualifications and thus had every right to bid for the oil contracts AND made the market more competitive to the benefit of our nation.

America is a capitalist nation. Competition is a part of our business and social fabric. The House Small Business Committee along with the Small Business Administration work to ensure that small businesses have access to a competitive market. We must ensure that full competition be encouraged in the energy industry. But most importantly, we must ensure that participation by capable small businesses be promoted through all the sales, exchanges, and purchases of Energy resources by the federal government.

The federal government is in a unique position to help small business & MBEs grow in this critical field. I am prepared to work with my colleagues on the Committee to develop legislation promoting innovative programs that assist small businesses to effectively compete in scientific, technical, environmental, and other energy related fields. Without these types of initiatives we are preventing small businesses and MBEs from competing in, and benefitting from federal procurement and the marketplace.

These actions make economic sense and are good for a continued healthy America. Thank you for this opportunity.

Mr. BARTON. Thank you, Congressman Hinojosa. We appreciate your testimony.

We now want to hear from the gentlewoman from Connecticut, Congresswoman DeLauro, for 5 minutes. Your statement is in the record in its entirety, and we ask that you summarize it.

**STATEMENT OF HON. ROSA L. DeLAURO, A REPRESENTATIVE
IN CONGRESS FROM THE STATE OF CONNECTICUT**

Ms. DELAURO. I thank the chairman and the ranking member and the rest of the committee for permitting me to testify this morning on this important issue. Just before my remarks, I just might want to make a comment because there has been a lot of discussion here this morning about the strategic quality of, if you will—or the national security issues mentioned with the Strategic Petroleum Reserve. I might call attention to folks that in 1999, there were several Republican leaders, including Mr. Armey, Mr. DeLay, and Mr. Blunt, who joined 35 other Republicans to introduce a bill that would have abolished the Reserve; in fact, the standard fare in the Vice Presidential race and the Presidential race, and Mr. Cheney has indicated, in fact, that he would have abolished the Strategic Petroleum Reserve. There seems to me to be a disjointed effort now to think about the Reserve in terms of its strategic nature when there were those who were just not a short time ago wanting to sell it off.

I come before you today, quite frankly, because of the Northeast, my part of the country. We have suffered in the last year as a result of the skyrocketing home heating oil prices and the plummeting supplies. I come before you on behalf of 678,000 Connecticut homes that are heated by oil.

This past winter families, seniors across the Northeast saw budgets stretched to the limit to accommodate outrageous home heating oil prices, forcing many to choose between basic needs like food and heat. In the cold of a New England winter, no one should ever have to make that kind of a cruel choice. I note that in the composition of the committee, there are people from the Northeast, people from the Midwest who experience that, but there are a lot of folks who come from some very warm climates who maybe don't understand the difficulty that people on the east coast are having.

With winter just around the corner, these families are confronted again with high home heating oil prices and limited supply. Government forecasters in the United States, the world's biggest en-

ergy user, are projecting a 12 percent increase in demand, a 25 percent rise in home heating oil bills nationwide from last winter, which was the warmest on record. In the Northeast home heating oil prices are approximately double the price last year, and supplies in the Northeast are 70 percent below where they were a year ago.

While this Congress continues to do little to address the concerns of families and seniors trying to heat their homes, in fact, the administration has acted quickly and efficiently in addressing the crisis. In July, the President showed leadership by creating the Northeast Home Heating Oil Reserve to reduce the risks presented by the shortages such as the one that I just spoke about. A 2-million-barrel reserve, half of which is stored in my district, will provide a safety net to many New Englanders.

Mr. Chairman, I visited the storage facility this past week, and I might add there were some good folks from Oklahoma who were there in charge of the process, Williams Energy, because it is a storage facility doing a darn good job there. The Reserve in the Northeast is now full, and a full 3 weeks ahead of schedule.

Mr. BARTON. Madam, there are not any bad folks from Oklahoma, they are all good folks.

Ms. DELAURO. Well, I would concur, and they are there doing a good job for those who live in the Northeast.

In September, the President, concerned with low crude and home heating oil stocks, directed the exchange of 30 million barrels of oil from the Reserve. The move is expected to add an additional 3 to 5 million barrels to home heating oil to that market.

Following that decision, a move that was praised by industry analysts, world leaders and residents of the Northeast, the price of crude oil dropped by almost 20 percent. It has meant relief for residents relying on home heating oil this winter and the confidence that, in fact, if we get into difficulty in the Northeast, we will have the Reserve close by.

The President also released \$400 million from the Low Income Home Energy Assistance Program, which provides emergency funds to all States, encouraging States to take steps now to help the crisis that can occur this coming winter. This is the largest release of LIHEAP emergency funds ever.

When you have a chance to do something, to lift the burden of families in this country, you do it. Releasing the Strategic Petroleum Reserve, creating the Northeast Home Heating Oil Reserve, releasing LIHEAP funds will, in fact, bring relief to families. It was the right thing to do.

We are facing lower prices of oil than we were a month ago. The President's actions are going to increase supply and decrease prices for American families.

The purpose of the hearing is supposed to question the administration's authority and efforts to reduce home heating oil costs and to bring heat to families. The argument would be moot if the Congress had acted promptly on the administration's suggestion for a comprehensive energy policy. Instead, most of the goals laid out by the administration have been untouched or unmet. Tax credits for domestic oil and gas production, energy efficiency, renewable energy, Congress has done nothing. The proposals on research in energy research, development in oil, gas, coal efficiency, renewables,

Congress has shortchanged the request by \$1.5 billion. This Congress has not even been able to pass legislation to authorize the use of their Reserve, create the Home Heating Oil Reserve, or trigger language that will allow us to use the Reserve.

The Energy Policy Conservation Act expired at the end of March. It awaits action in the Senate. We need to be serious about making a commitment to comprehensive energy policy on both sides of the aisle. I appreciate the bipartisan nature of this committee and its willingness to be able to do that. That is what our job is and not to politicize the issue.

I would add one more point, because the Jones Act has been mentioned here today. We need to take a very close, hard look at that effort as well and look at whether or not—because industry would have to pay insurance prices and doesn't want to have to do that; or maybe, in fact, because the oil abroad will get a higher dollar amount for that than it is going there rather than here; or maybe, in fact, we do need to do something in a bipartisan way to look at how we can get that oil from the Gulf and get it to the Northeast, but it can't be on the basis of politics and fighting against one another, but what is in the best interests of the people who live not only in the northeastern part of this country, but all over this country. Thank you.

[The prepared statement of Hon. Rosa L. DeLauro follows:]

PREPARED STATEMENT OF HON. ROSA L. DELAURO, A REPRESENTATIVE IN CONGRESS
FROM THE STATE OF CONNECTICUT

I would like to thank Chairman Barton and the rest of the Committee for permitting me to testify on this very important issue. Too many people suffered in the Northeast last year as the result of skyrocketing home heating oil prices and plummeting supplies

I come before you today on behalf of the estimated 678,000 Connecticut homes heated by oil. This past winter, families and seniors across the Northeast saw their budgets stretched to the limit to accommodate outrageous home heating oil prices, forcing many to choose between basic needs like food and heat. In the cold of a New England winter, no one should ever have to make that kind of cruel choice.

With this winter just around the corner, these families are confronted again with high home heating oil prices and limited supply. Government forecasters in the U.S. are projecting a 12 percent increase in demand—and a 25 percent rise in home heating oil bills nationwide—from last winter, the warmest on record.

In the Northeast, home heating oil prices are approximately double that of last year and supplies are 70 percent below where they were a year ago. Constituents in my district are now paying \$1.33 per gallon for home heating oil.

While this Congress continues to do little to address the concerns of families and seniors trying to heat their homes, the Administration has acted quickly and efficiently in addressing this crisis.

Back in July, the President showed great leadership in creating a Northeast home heating oil reserve to reduce the risks presented by home heating oil shortages, such as the one that occurred last winter. The two million barrel reserve, half of which is stored in my district, will provide a safety-net to many New Englanders. The Northeast Reserve is now full—a full 3 weeks ahead of schedule.

In September, the President, concerned with low crude and home heating oil stocks, directed the exchange of 30 million barrels of oil from the Strategic Petroleum Oil Reserve. The move is expected to add an additional 3-to-5 million barrels to the home heating oil market.

Following that decision—a move praised by industry analysts, world leaders and residents of the Northeast alike—the price of crude oil dropped almost 20 percent. This has meant relief for residents relying on home heating oil this winter—and those who are still facing high prices at the pump.

The President also released \$400 million dollars from the Low Income Home Energy Assistance Program (LIHEAP), which provides emergency funds to all States, encouraging States to take steps now to help low-income households cope with high

fuel prices this coming winter. This is the largest release of LIHEAP emergency funds ever.

When you have a chance to do something to lift the burden of families, you do it. Releasing the Strategic Petroleum Reserve, creating the Northeast Home Heating Oil reserve, and releasing LIHEAP funds will bring relief to relies and it was the right thing to do.

As a result of the President's actions we are facing lower prices of oil than we were a month ago. His actions are going to increase supply and decrease prices for American families.

The purpose of this hearing is supposed to question the Administration's authority and efforts to reduce home heating oil costs and bring heat to families. This argument would be a mute point if this Congress had acted promptly on the Administration's comprehensive energy policy.

Instead, most of the energy goals laid out by the Clinton/Gore Administration have either been untouched or unmet.

The Administration has proposed tax credits for domestic oil and gas production, energy efficiency, and renewable energy—yet Congress has done nothing.

The Administration has proposed investments in energy research and development in oil, gas, coal, efficiency, renewables, and nuclear energy—Congress has shortchanged their request by \$1.5 billion.

This Congress has not even been able to pass legislation to fully authorize the use of the Strategic Petroleum Reserve, create a Northeast home heating oil reserve, or the trigger language that would allow us to use this Reserve. The Energy Policy Conservation Act, which expired at the end of March, still awaits action in the Senate.

If this Congress, was serious about making a commitment to a comprehensive energy policy that reduces prices in home heating oil and at the pump, it would have passed these proposals a long time ago.

In fact, rather than politicizing the Administration's efforts to bring heat to Americans trying to heat their homes this winter, we should be holding a real hearing that looks into the failure of this Congress to meet the basic energy needs of American families.

My only hope is that this Congress relies less on their hopes for a warm winter, and more on a comprehensive energy policy. The families and seniors anticipating another long, cold winter demand it.

Thank you.

Mr. BARTON. I would like to point out to the gentlewoman, we passed the EPCA reauthorization on April the 12th in the House on a bipartisan basis with the Northeast Fuel Oil Reserve that was put in at the direct request of Congressmen Markey, Fossella and Barton.

Ms. DELAURO. It was stripped out of the energy bill and the appropriations bill when it did come to the House, but it is now—you are right, it is in the Senate where it is being held up. I thank the chairman.

Mr. BARTON. I think Mrs. Cubin was next.

Mrs. CUBIN. Thank you, Mr. Chairman.

Mr. KNOLLENBERG. I yield to Mrs. Cubin.

Mr. BARTON. Congresswoman Cubin for 5 minutes.

**STATEMENT OF HON. BARBARA CUBIN, A REPRESENTATIVE
IN CONGRESS FROM THE STATE OF WYOMING**

Mrs. CUBIN. Thank you, Mr. Chairman and committee, for inviting me to testify today on the administration's planned swap of 30 million barrels of crude oil from the Nation's Strategic Petroleum Reserve. I am sorry that Representative DeLauro has to leave, because I think that one thing that has been left out of her analysis of the problem is that part of the reason we have a lack of supply is a direct result, at least in part, of environmental extremism that doesn't allow us to go on to public lands to explore and produce oil. We have vast volumes of reserves on high desert plains that, in my

eye, are very beautiful, but in somebody else's eye might not be beautiful, that are not allowed to be explored or drilled because of extreme Endangered Species Act interpretation and other environmental laws. So I would ask that people sit down at the table, people in the Northeast would sit down at the table with us and talk about some of the problems we have in getting access to public lands.

On the Resources Committee, I chair a subcommittee with jurisdiction over minerals, energy, and included Federal mineral leasing laws. I held a hearing 18 months ago to review the administration's proposal at that time to use royalty oil taken in kind from the outer continental shelf leases in the Gulf of Mexico to partially fill the Strategic Petroleum Reserve, which I will call SPR. The time was ripe then, as the price was quite low. It was about \$13 per barrel for west Texas intermediate benchmark crude. The DOE proposed to take some 28 million barrels in kind, albeit the program was suspended after only 11 million barrels, because global demand had recovered, and supplies were tight. Thus began the sharply higher priced trend that we are seeing today, which the recent SPR swap program was intended to blunt.

Mr. Chairman, it is clear to me that SPR swaps can have a very, very short-term effect on crude prices, as little as a few days, at most a week or 2, but that is the extent of it. Why such a short response? Because demand-side pressures swamp such piddly increments of supply, obviously.

Now, I am not an economist, but even I can do the simple math. I used to teach math, and I hope everybody will look at this; I have included it in my statement, the facts about import and export oil in the United States. The Energy Information Administration reports that the United States imported 9,455,000 barrels of crude oil per day in the year 2000, which is the last month of actual data, while simultaneously we exported 9,000 barrels per day, for a net import of crude oil of 9.446 million barrels per day. Then, when you take into consideration the million barrels of refined product, including heating oil that we import, the total of imports is 10,446,000 barrels per day, which means that the 30 million barrels of crude that the administration wants to swap represents only 3 days of imports, 3 days.

While I was not in Congress when the SPR was created, although I invented oil—forgive me, forgive me for that—I am well aware of the purpose for which this reserve is to be set aside, and serving as a buffer to oil market conditions is not it. It is for strategic protection. The only thing strategic about this swap is with respect to the Vice President's election campaign. Incredibly, as the Wall Street Journal story attests, though, the administration has had problems getting even this oil to refiners to distill into heating oil and diesel fuel, because our refinery capacity in the United States is at its capacity. Furthermore, a dear colleague letter that was passed around last week that went over my desk asking me to sign a letter to the President urging him to disallow export of U.S. heating oil supplies to foreign markets impressed me with the lack of wisdom in it. But if other nations were to reciprocate in kind in this policy, it would exacerbate the severe supply problem that we have now, and particularly for the Northeast.

So think about it. If we are net energy, or net heating oil, net oil importers of distilled and residual fuel oil as well as crude, we have to be very careful about barriers that we set up to free trade so that our trading partners don't do the same thing to us. We could end up in a much worse position if they decided to quit exporting to us because we quit exporting and interfered with free trade.

I mentioned earlier royalty in kind, Mr. Chairman. As you know, a dispute in the other body, largely over the RIK provision, is keeping EPCA reauthorization from being considered on the Senate floor.

Mr. Chairman, I can't see my lights. I don't know how much time I have. Oh. So I think I have exactly the right amount of time to finish.

I support Senator Mikulski's position, which would give the Secretary of the Interior more authority to expand the program whereby oil and gas royalties on Federal leases are paid in volumes of oil and natural gas, rather than in cash, particularly on the OCS. If the Feds were to aggregate their royalty volumes from many leases, we would have a market power which translates into increased value for the oil and gas.

In a recent pilot program, the Minerals Management Service has taken natural gas in kind from offshore Texas leases and sold it to GSA for use by Federal facilities. In fact, the heating oil that heated—our office buildings were heated by some of this oil.

The Interior Appropriations Act signed into law last week has a short-term provision for RIK enhancement, but the EPCA language is better and worthy of House approval if the Senate can break the logjam.

In the 107th Congress, we have to dedicate ourselves to creating a national energy policy that takes on the issue of domestic supply head on. My State of Wyoming is ready and willing and able to provide copious amounts of natural gas, including coalbed methane, coal and oil, to help balance that supply and demand equation.

Thank you, Mr. Chairman. I will be happy to answer any questions.

Mr. BARTON. Thank you.

The gentleman from Michigan, Mr. Knollenberg is recognized for 5 minutes.

STATEMENT OF HON. JOE KNOLLENBERG, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MICHIGAN

Mr. KNOLLENBERG. Mr. Chairman, thank you very much for holding this hearing. I thank you, and I thank Ranking Member Boucher as well. It is timely, and it is necessary.

As a member of the House Energy and Water Appropriations Subcommittee, and as a representative from the auto-producing State of Michigan, I have a very keen interest in today's hearing. I would like to have heard, obviously, from Secretary Richardson, who I understand was invited here but could not come. After leading the charge to release oil from the SPR, it is unfortunate that he does not consider this hearing to rise to the appropriate level of importance.

The SPR and the Nation's overreliance on foreign oil supplies impacts each and every American. This subject deserves all of the attention that this subcommittee is affording it today, and more. Releasing oil from the SPR puts both energy and national security at risk. It does not solve our national overreliance upon foreign oil supplies. It is a dangerous move by the administration in an attempt to temporarily reduce oil/gas prices for what can only be deemed political gain in the November election.

Chairman Barton and others are right to raise the question of whether this release of oil from the SPR rises to the level intended in the authorizing legislation. The President has not declared a national emergency, nor has he told the American people that the current situation is a severe supply or price disruption. World markets have plenty of oil, as evidenced by OPEC's production increases over the last weeks. Instead, the administration claims that this is only a swap, with no real loss of oil from the reserves. A year from now, we will know whether the SPR has been replenished to its intended level.

Although I hope that the price of oil 12 months from now is less than \$35 a barrel, that is by no means guaranteed. As anyone who follows closely, as I do, the changes which transpire rapidly and dangerously on the international level, this release is a gamble with American security. Recent events in the Middle East exemplify just how delicate the situation can be.

According to the most recent data from the Energy Information Agency, domestic production has dropped 17 percent since 1992, while overall oil consumption is up 14 percent. Those are troubling numbers. The U.S. is now more than 55 percent reliant upon foreign oil supplies. But that need not be the situation. America has substantial reserves of oil and natural gas, both in the outer continental shelf and in Alaska. Careful and environmentally responsible exploration and drilling in these areas can and should be allowed. The amount of land in question is minimal, and we have the technology to recover the oil with essentially zero environmental impact. And U.S. refineries are operating at near capacity, as high as 96 percent or more. Any increase in the upstream supply of crude oil will have little, if any, impact on the roughly 16 million barrels per day that the 155 U.S. refineries can churn out.

I might reference another point when it comes to refineries, and this applies to Mr. Shimkus' State of Illinois. This Nation's sole remaining uranium refinery is on the immediate verge of closing within the next month, yet, despite repeated requests to the administration, they have failed to answer, and that is emblematic, I think, of this administration's failed energy policies when nuclear produces over 20 percent of our energy needs.

Such high capacity is, in part, due to the need to increase inventories of home heating oil for the upcoming winter season, a season that, by the way, NOAA has just recently warned will mark a return to colder temperatures in both the Northeast and Midwest, yet the record high capacities are also due to the fact that no new refineries have been built in the U.S. for several years now. Burdensome mandates and all too often scientifically flawed regulations put forth by the administration, in particular by the Environmental Protection Agency, have stymied any new investments in

infrastructure. Many have claimed that the energy problems the Nation is experiencing are the result of the Clinton-Gore Administration's failure to develop and pursue a sound national energy policy. The last time I looked, the administration is in charge of the Department of Energy.

Actually, it appears instead that they have what can only be termed as an anti-energy policy. Their actions have served to thwart and cut our energy supply and drive up costs. They pit one energy source against another and create constant obstructions of roadblocks with volume after volume of regulation.

Petroleum production plays a much greater role in the economy than just gasoline and home heating oil. Increases in the price of oil can therefore have a ripple effect on the prices of other goods. That is why it is important to reduce our reliance on imported oil and to fully support clean coal, hydro and nuclear power as a means of meeting the Nation's energy demands. It is also why we need to invest in reasonable research and development in the development of new energy technologies, not only the solar and the wind power projects that this administration lavishes millions and billions of dollars on, investments yet to show very much promise when it comes to contributing to increasing our overall energy demands. It is precisely the antienergy policy of the Clinton-Gore Administration which has led to the current situation of high oil and natural gas prices. Unfortunately, it is the American people who are now being forced to bear the cost of this administration's antienergy policy.

Again, I want to thank the subcommittee for affording me the time here today. I do think this is very important, and I appreciate very much you taking the time to make a case for our investigating what I believe is a problem; not just a long-term problem, it is a short term problem, and we have to do something about it. I thank the chairman.

[The prepared statement of Hon. Joe Knollenberg follows:]

PREPARED STATEMENT OF HON. JOE KNOLLENBERG, A REPRESENTATIVE IN CONGRESS
FROM THE STATE OF MICHIGAN

INTRODUCTION

Thank you Chairman Barton, Ranking Member Boucher and other Members of the Commerce Energy and Power Subcommittee for affording me the opportunity to speak today. Thanks are also due to the panelists for taking time out of their busy schedules. I look forward to your testimony.

As a Member of the House Energy & Water Appropriations Subcommittee, and as a Representative from the auto-producing state of Michigan, I have a keen interest in today's hearing. I would have liked to have heard from Secretary Richardson who declined to be here today. It is my hope that his absence does not indicate that matters involving the SPR do not rise to the appropriate level of importance for the Administration. I for one consider the topic extremely important. The Strategic Petroleum Reserve and the nation's over-reliance on foreign oil supplies impacts each and every American. The subject deserves all the attention that this subcommittee is affording it today.

Releasing oil from the SPR puts both energy and national security at risk. It does not solve our national over-reliance upon foreign oil supplies. It is a dangerous move by the Administration in an attempt to temporarily reduce oil/gas prices for what can only be political gain in the November election.

AUTHORITY FOR THE SPR RELEASE

Chairman Barton and other Members are right to raise the question of whether this swap of oil from the SPR rises to the level intended in the Energy Policy Con-

servation Act authorizing the Reserve. The President has not declared a national emergency, nor has he told the American people that the current situation is a severe supply or price disruption. World markets have plenty of oil, as evidenced by OPEC's production increases over the past few weeks.

Instead, the Administration claims that this is only a "swap", with no real loss of oil from the reserves. A year from now, we will know whether the SPR is replenished to its intended level. And although it is to be hoped that the price of oil twelve months from now is less than \$35 a barrel, that is by no means guaranteed. As anyone who follows closely, as I do, the changes which can transpire rapidly and dangerously on the international level, it is only prudent to restore the SPR to its pre-release levels in as short a period as possible.

Recent events in the Middle East show clearly just how delicate the situation there can be. Oil prices leapt after the tragic bombing of the U.S.S. Cole in Yemen. Indeed, it is for emergencies such as drastic supply interruptions or military engagements that the Strategic Reserve was created. Its 571 million barrels in the salt domes of Louisiana and Texas represents only five weeks of total demand and only two months of foreign imports in the event of a disruption. It was for times of national crisis that the SPR was established, not to control market fluctuations.

Prices are without a doubt high, especially in relation to just a short year ago when crude was nearer \$10 a barrel. And there is no question that heating oil reserves for the coming winter months are a concern. But market price fluctuations are different from supply interruptions and national emergencies. The President and the Administration know the difference, yet they choose to ignore it. They seem to place more weight on maintaining control of the White House, than on protecting America's energy and national security.

SUMMERS/GREENSPAN VIEWS

Even the Administration's top financial and economic advisors recognize the flaws in opening up the SPR. We've all seen the *Wall Street Journal* article covering the memo from Treasury Secretary Lawrence Summers to President Clinton advising against any release of oil. Secretary Summers was right when he said opening the SPR, "would be a major and substantial policy mistake."

Even the man most-often credited with orchestrating the nation's economic prosperity over the past several years, Alan Greenspan, agrees. The nation entrusts these men to make decisions on the money supply, interest rates and national debt, only somehow not when it comes to this matter.

DOMESTIC OIL SUPPLIES

According to the most recent data from the Energy Information Agency, domestic oil production was 5.9 million barrels a day while imports were 9.1 million barrels a day. Compare that to 1992 when we had domestic production of 7.2 million barrels a day and imports of 6.1 million barrels. Our domestic production has dropped 17% since 1992 while overall oil consumption is up 14%. Those are truly troubling numbers. The U.S. is now over 60% reliant on foreign oil supplies.

But that need not be the situation. America has substantial reserves of oil and natural gas, both in the outer continental shelf and in Alaska. Potentially as many as 7.7 billion barrels in Alaska alone.

Careful and environmentally-responsible exploration and drilling can and should be allowed in limited areas of the Arctic National Wildlife Reserve in proximity to the existing oil-production areas. The amount of land in question is minimal and we have the technology to recover the oil with essentially zero environmental impact.

REFINERY CAPACITY & REGULATIONS

Another point that requires mentioning is that U.S. refineries are operating at near capacity—as high as ninety-six percent or more. Any increase in the upstream supply of crude oil, such as a release from the SPR, will have little if any impact on the roughly 16 million barrels per day that the 155 U.S. refineries can churn out.

Such high capacity factors are in part due to the need to increase inventories of home heating oil for the upcoming winter season. A season that by the way the National Oceanographic Atmospheric Administration has just recently warned will mark a return to colder temperatures in both the Northeast and Midwest. Yet the record high capacities are also due to the fact that no new refineries have been built in the U.S. for several years now. Burdensome mandates, and all-too-often scientifically-flawed regulations put forth by the Clinton-Gore Administration, in particular

by the Environmental Protection Agency, have prevented the industry from investing in any new refining capacity.

While refining capacities in the petroleum industry are near maximum, the Administration has ignored similar difficulties in the front end of the uranium fuel cycle. This issue has not received the attention it deserves. Past actions on the part of the federal government have profoundly impacted U.S. uranium mining and conversion—the equivalent of refining for commercial nuclear power. The unintended consequence of these actions has been a drastic reduction in prices, threatening the survivability of the U.S. firms involved. Loss of our domestic mining and conversion capabilities could seriously impact our national energy security.

Earlier this year, gasoline prices in my home state of Michigan and indeed much of the Midwest, hit more than \$2.00 a gallon for several weeks. Part of the price escalation can be attributed to pipeline and refinery interruptions. Somewhat surprisingly, those supply interruptions did not merit consideration of an SPR release by the Administration.

Yet that isn't the only reason. EPA mandates on gasoline resulted in the astounding situation where a driver traveling from St. Louis to Chicago would have passed through four different "gasoline control zones". With three grades required for each zone, that means refiners must produce twelve different blends for just a 300 mile stretch of highway. Just one example of how the Clinton-Gore Administration has over-regulated the nation into crisis.

RE-BIDDING OF CONTRACTS

Next we learn that the bidding process used by DoE to select companies to take the oil from the SPR was flawed. It seems that as many as 7 of the 30 million barrels to be released was awarded to companies without the requisite financial capabilities and without any capabilities to actually transport or refine the oil. It is unfortunate when the Department of Energy puts such a high priority on releasing oil from our national reserves but then fails to execute the required diligence in selecting bidders. The decision to swap oil from the reserves was a bad one, but to learn that it was done improperly only adds insult to injury.

ADMINISTRATION'S ANTI-ENERGY POLICY

With petroleum and natural gas demand outstripping production and inventories, the increase in prices is only to be expected. Many have claimed that the energy problems the nation is experiencing, and is likely to feel even more acutely in the coming winter months, are the result of the Clinton-Gore Administration's failure to develop and pursue a sound national energy policy.

Actually, it appears instead that they have what can only be termed an **anti-energy policy**. Their every action has served to thwart and cut our energy supply and drive up costs. They pit one energy source against another and create constant obstructions and road blocks with the volumes and volumes of regulations, rules, guidances, and executive orders that they issue.

The Vice President has stood resolutely behind his 1993 book *Earth in the Balance*. The very same book where he stated, "*We know that the automobile's cumulative impact on the global environment is posing a mortal threat to the society of every nation that is more deadly than that of any military enemy we are ever again likely to confront.*" It would appear that Mr. Gore equates the nation's primary mode of transportation, a cornerstone of the American economy, with the likes of Osama bin-Laden and Saddam Hussein. Such statements make the Vice President's about face on oil prices and his resulting call to release the reserves ever the more surprising.

And petroleum products play a much greater role in the economy than just gasoline and home heating oil. Increases in the price of oil can therefore have a ripple effect on the prices of other goods. That is why it is important to reduce our reliance on imported oil and to fully support clean-coal, hydro and nuclear power as means of meeting the nation's energy demands.

It is also why we need to make reasonable investments in research and development of new energy technologies, not only the solar and wind power that the Administration lavishes taxpayer dollars upon, year after year. Investments that have yet to show very much promise when it comes to contributing to our overall energy demands.

It is precisely the "anti-energy" policy of the Clinton-Gore Administration which has led us to the current situation of high oil and natural gas prices. Unfortunately, it is the American people who are now being forced to bear the cost of this Administration's anti-energy policy.

CLOSING

Again, I thank the Subcommittee for affording me time to speak here today. It is my hope that the Administration will see the error in their decision to release oil from the Reserve for the purposes of manipulating short term market fluctuations. What is needed is a real domestic energy policy, one that reduces our dependence on foreign oil through environmentally sound exploration and development of our petroleum resources, one that does not stifle our proven methods of energy production, and one that promotes investment in technologies that will provide for the nation's future energy needs.

Thank you.

Mr. BARTON. I thank the gentleman from Michigan.

The Chair has no questions for this panel.

The Chair recognizes Mr. Boucher.

Mr. BOUCHER. Thank you, Mr. Chairman. In the interest of time, I am not going to ask questions of this panel either, but I would like to thank them for joining us here.

Mr. BARTON. Does the gentleman from Oklahoma wish to ask questions?

Mr. LARGENT. No questions.

Mr. BARTON. Does the gentleman from Illinois wish to ask questions?

Mr. SHIMKUS. No, Mr. Chairman.

Mr. BARTON. Does the gentleman from Louisiana wish to ask questions?

Mr. TAUZIN. No questions.

Mr. BARTON. Well, I don't believe it. The first panel we have ever had that didn't get one question asked. Because you all told the truth, and were eloquent in telling it. We appreciate you appearing before the subcommittee, and you are excused at this point in time.

We want to hear from our second panel now.

Our next panel consists of Robert S. Kripowicz, Acting Assistant Secretary for Fossil Energy, Department of Energy; Roger Majak, Assistant Secretary for Export Administration, U.S. Department of Commerce; and a representative from the Department of the Treasury.

Gentlemen, welcome.

Assistant Secretary Kripowicz, we are going to start with you. We are going to recognize you for such time as you may consume. We will put your statement in the record in its entirety and ask you to try to summarize, but, obviously, the purpose of this hearing is to really get into the details of this swap of SPR, so we want to give you sufficient time to explain the principles involved, and then we will go to Mr. Majak. Welcome to the subcommittee.

STATEMENTS OF HON. ROBERT S. KRIPOWICZ, ACTING ASSISTANT SECRETARY FOR FOSSIL ENERGY, DEPARTMENT OF ENERGY; AND HON. R. ROGER MAJAK, ASSISTANT SECRETARY FOR EXPORT ADMINISTRATION, U.S. DEPARTMENT OF COMMERCE

Mr. KRIPOWICZ. Thank you, Mr. Chairman. I will summarize.

Mr. BARTON. You really need to put the microphone close to you, sir.

Mr. KRIPOWICZ. Mr. Chairman and members of the subcommittee, the administration has been concerned about stock levels of critically needed fuels, such as heating oil and diesel fuel,

since last winter. Many of you may recall that this past January temperatures in New England plunged, and prices for heating oil increased dramatically. Many consumers not only faced unexpectedly high heating oil bills, but, for a few very tense weeks, they faced the very real possibility of not having enough fuel to heat their homes.

The President and this administration are determined to do everything they can to protect Americans from a repeat of last winter.

On July 10 of this year, President Clinton directed Secretary Richardson to establish an interim heating oil reserve, 2 million barrels, that would provide an emergency cushion for this winter. He called on Congress to enact legislation that would make the Reserve permanent and provide an appropriate trigger for releasing the heating oil if Americans were threatened. I am pleased to report today that we have completed our part. As of last Friday, the heating oil reserve is fully stocked for this winter, 3 weeks ahead of schedule.

Today, we are releasing for public comment a draft of the process we would follow if a crisis this winter requires the Reserve to be used. The only thing missing is a regionally specific trigger, and we remain hopeful that Congress will take action on this before leaving town.

Stock levels, however, have continued to lag well behind last year. Throughout the summer, the President looked for other actions he could take to protect American families this winter.

He directed the Department of Health and Human Services to release \$400 million in low-income home energy assistance program funds, the largest ever emergency funding release of its kind.

He asked the Environmental Protection Agency to help States identify ways to use more and different kinds of home heating oil while minimizing environmental consequences. This could help to further build home heating oil inventories.

He directed Federal agencies to make early contractual commitments to purchase heating oil throughout the winter so wholesalers will have the confidence to build inventories in advance.

He asked State public utility commissions to ensure that factories and businesses that use distillate heating oil as backup fuel keep adequate reserves. At least New York and New Jersey have done that.

These were virtually all of the options available to the President for this winter, with one exception, and that was the use of the Strategic Petroleum Reserve. The President held open that option while we continued to monitor the supply situation. On September 22, he felt he could wait no longer. Winter was approaching and stocks of heating oil and other fuels were still at abnormally low levels. In the Northeast, where one out of three families rely on heating oil to stay warm, distillate inventories were 49 percent lower than last year. In New England, heating oil stocks were 65 to 70 percent lower than last year.

With the stock situation still at critically low levels, the President directed Secretary Richardson to release oil from the Reserve under authorities contained in section 160(a) of the Energy Policy

and Conservation Act. These authorities authorize an exchange of crude oil, not a sale.

In essence, the provision permits the Secretary of Energy to exchange oil from the Reserve for the purpose of acquiring additional oil. That is the way we structured our solicitation. Companies acquiring oil from the Reserve this fall must commit to return it, plus a bonus, next fall. This action will help protect Americans this winter, and it will add to our energy security next winter and beyond.

Will we succeed in adding 3 to 5 million barrels of distillate fuel to stock levels this winter? We believe so. Our analysts tell us that the models—and past experience—are good indicators that this will happen. They tell us that it is our best chance to make it happen. But obviously, the market is complex, and no one can say with absolute certainty. But consider this: What if Americans are confronted this winter with a life-or-death situation and the President had not used all the means available to him?

Mr. Chairman, the oil market remains fragile today, and the scenario has played out much as we expected. Refineries are entering into their turnaround periods, dropping their output slightly. Stock levels remain low, with heating oil inventories down by another 800,000 barrels from last week, a 1.7 percent drop.

But today the market, and perhaps most importantly the market psychology, is a lot different than a month ago. We are beginning to move 23 million barrels of crude oil from the Reserve into it. The first deliveries began last Friday, and more oil is being delivered today, and a total of 4 million barrels will be delivered in October, before the original contract delivery dates.

The difference between current distillate prices and those on the futures market is much less today, the market is much less what they call “backwardated”, and that creates some incentive to build inventories.

Although refinery utilization has dropped to about 91 percent, distillate fuel production last week was actually up by about 140,000 barrels per day, as refiners increased the portion of the barrel being refined into distillate fuel oil. We are not out of the woods yet, but Americans should recognize that we are exhausting every option to encourage higher inventories and ensure their well-being for the winter.

I do recognize that there have been some questions about the way we have conducted the exchange competition, and my formal statement outlines the details of the process, but I would like to make three key points:

First, at no time during the solicitation was the taxpayer at risk of losing oil from the Reserve. While initially we waived the front-end bid bond requirement, to give the largest number of bidders the best opportunity to move oil quickly into the market, no oil would leave the Reserve until we had an irrevocable letter of credit for its full value. The government and the taxpayer were protected throughout the process.

This type of arrangement has worked successfully in the government’s interest during past exchanges, for example, in the royalty-in-kind initiative.

The second point is that we did not award contracts until we had evidence that the successful offerors had a reasonable opportunity

to move the oil into the market, either themselves or in arrangements with other parties. Even though three of the bidders were unknown to us at the time the bids arrived, we determined that one had experience in past energy trading and the other two had serious discussions under way with companies that could move the oil. Only then did our contracting officer deem these to be responsible bids.

It is important to recognize that energy traders can play just as key a role in moving oil into the market as companies that own refineries, and, in fact, other successful offerors, in this exchange and in other SPR oil releases, have been traders.

The last point is that we are moving more oil into the marketplace in a shorter period of time than ever in the history of the SPR. More oil will be delivered by the end of November than was delivered during the Desert Storm drawdown in 1991. The oil we currently have under contract, 23 million barrels, is a third more than the 17 million barrels released then. Three million of those barrels would not have been included had we arbitrarily ruled out the three offerors that some have questioned.

In short, we believe the exchange process is proceeding well.

Let me make one final point. I would like to compliment our career professionals at the SPR office, both here in Washington and in the field. They have done an excellent job in responding to the President's direction. Oil is moving into the market sooner than we planned. We have solid guarantees in place to replenish the oil and to add to the Reserve next year. Because of them, Americans will be better protected this winter.

That completes my opening statement.

[The prepared statement of Hon. Robert S. Kripowicz follows:]

PREPARED STATEMENT OF HON. ROBERT S. KRIPOWICZ, ACTING ASSISTANT
SECRETARY FOR FOSSIL ENERGY, U.S. DEPARTMENT OF ENERGY

Mr. Chairman and Members of the Subcommittee: When Secretary of Energy Bill Richardson directed the exchange of crude oil from the Strategic Petroleum Reserve (SPR), he did it to increase critically needed fuel supplies, especially heating oil in the Northeast, and to help consumers make it through a cold winter. In addition, this action will ultimately add oil to the SPR, increasing our overall energy security.

We are already moving 23 million barrels of crude oil into an extremely tight market. The first crude oil from the Reserve started moving last Friday, and more is scheduled for delivery today. Refineries are maintaining high levels of product output, and in a separate action, we now have in place a fully stocked and ready-to-use emergency reserve of heating oil in the Northeast.

In short, Mr. Chairman, while we are not yet out of the woods, Americans are significantly more protected today from a possible energy shortfall this winter than they were a month ago.

RATIONALE FOR THE EXCHANGE

The President made the decision to carry out the oil exchange because of concerns that lagging petroleum product inventories could create potentially severe hardships for many American families this winter. Across the country today, distillate inventories, which include heating oil, are 21 percent lower than they were a year ago. In the Northeast, where 37 percent of families use heating oil to stay warm, distillate inventories are lower still: 49 percent less than last year's levels. In New England, heating oil inventories are closer to 70 percent lower than last year.

While global oil production increases have added three-and-a-half million barrels of oil per day to the world market, due in part to the Administration's diplomatic efforts, demand continues to siphon off most of the extra barrels before they move into inventories. Thus, world and U.S. crude stocks remain very low, and stocks of heating oil and other distillate fuels are at critically low levels.

Stock builds are critical to the Northeast; during the course of winter up to 17 percent of the region's heating oil will come from inventories. During cold snaps, drawdowns of inventories can constitute an even greater percentage of local supplies. Why do we believe that a temporary infusion of crude oil into the market will lead to additional heating oil supplies this winter? There are complicated and detailed answers involving world energy market interactions, refining yields, and seasonal market shifts that could be provided, but let me focus on the basic issues:

- **The crude oil was needed in the market:** Crude oil inventories worldwide have been low and did not appear likely to increase in the near future unless action was taken;
- **Refineries could increase heating oil output at this time:** U.S. refineries were about to enter the fall season when their configurations change to increase distillate yield relative to gasoline yield, and gasoline output can be maintained by use of more volatile blendstocks than in the summer. This is also a time when refineries do maintenance, both discretionary and non-discretionary. Discretionary maintenance can be delayed when market conditions offer appropriate incentives.
- **Middle distillates (diesel fuel, heating oil, jet fuel, and other transportation fuels) account for about 25 percent of the total refined output:** Heating oil is usually about 10 percent of the total output (40 percent of the distillate yield) but the other distillate products can be used for heating fuel when demand requires. Having an increased output of all middle distillates would increase the cushion for cold spells.
- **Most of the crude oil we are exchanging from the SPR is light, sweet crude oil** (25 million of the 30 million barrels initially awarded; 18 million of the 23 million barrels currently under contract). In the refining process, this type of crude oil offers the highest yields of critically needed distillate products.

Considering all these factors, the Energy Information Administration estimated that an additional 3-5 million barrels could be added to distillate fuel inventories as a result of the SPR exchange.

STATUTORY AUTHORITIES FOR EXCHANGING RESERVE OIL

There is clear legislative authority in the Energy Policy and Conservation Act (EPCA) 42 U.S.C. 6201 et seq., that authorizes the Secretary of Energy to exchange oil from the Strategic Petroleum Reserve.

Section 160(a) states that:

*The Secretary is authorized, for purposes of implementing the Strategic Petroleum Reserve Plan—to place in storage, transport, or **exchange**:*

(1) crude oil produced from Federal lands, including crude oil produced from the Naval Petroleum Reserve to the extent that such production is authorized by law;

(2) crude oil which the United States is entitled to receive in kind as royalties from production on Federal lands, and

*(3) petroleum products acquired by purchase, **exchange**, or otherwise. [emphasis added]*

One of the primary “*purposes of implementing the Strategic Petroleum Reserve Plan*” is to acquire additional crude oil for the Reserve. The exchange solicitations issued by the Department on September 25, and in modified form on October 16, explicitly state that the companies awarded contracts must return more crude oil of comparable or higher quality than they received. Contracts were awarded on the basis of offers that would return the highest value of additional specification-grade crude oil to the Reserve. Therefore, the requirement of Section 160(a) will be met, and the exchange is being carried out within the Department's existing legal authorities.

Crude oil exchanges from the Reserve have been used before. On two occasions, including one instance this summer, Reserve crude oil has been exchanged with companies facing disruptions in crude oil deliveries because of transportation problems (a pipeline blockage in 1996; a shipping channel blockage this past June).

In 1998, the Department exchanged a lower-quality crude oil for a higher quality crude that better matched the Reserve's specifications.

Currently, exchanges are being used to supply the Reserve with specification-quality crude oil in the Royalty-in-Kind initiative (where a portion of federal royalty oil from production in the Central Gulf of Mexico is being used to re-fill the SPR). Because of market conditions, it was advantageous for both the government and the companies to renegotiate delivery dates for several of these contracts, allowing the contractors to have more time in exchange for more oil later. The department effec-

tively exchanged 16 million barrels of oil due in 1999 and 2000 for 18 million barrels of oil due in 2000 and 2001.

THE ONGOING PROCESS FOR EXCHANGING CRUDE OIL

The solicitation, bidding, and contract award process was developed by staff in the Department's Strategic Petroleum Reserve Office. It was designed to meet two overarching goals: (1) to move Strategic Reserve crude oil into the market as quickly as possible, and (2) to acquire the most crude oil for the Reserve while assuring adequate protection to the government and the taxpayer for the value of the SPR oil.

To encourage as many bidders as possible—including both large and small companies that might be able to take delivery of the oil or arrange trades that could move the oil quickly into the market—the SPR office elected to forego an upfront bid bond requirement and instead required necessary financial protections to be in place prior to delivering the SPR crude oil. Past experience had indicated that a requirement to provide a bid bond or earnest money could add to the time and expense and make it difficult for many companies, especially small businesses, to prepare responsive bids.

As protection for the taxpayer, a letter-of-credit from a certified financial institution for the full value of the crude oil was required within 5 working days after a contract was awarded.

This is an important point, Mr. Chairman. At no time in the process was the government at risk of losing the value of any oil in the Reserve. No oil would be delivered without the protection of an irrevocable letter-of-credit.

On September 25, 2000, the Department released its exchange solicitation. In addition to the letter-of-credit requirement, the SPR contracting office also required other certifications from each offeror. These certifications attested to the independent nature of the exchange offer along with the disclosure of certain possible prior criminal or civil judgments. While the exchange process is not a procurement action under Federal acquisition guidelines, the SPR office also consulted the listing of companies debarred or suspended from Federal procurements prior to making contract awards.

The SPR office also reviewed all publicly available information on those bidders who were unfamiliar to the contracting office. In the case of two offerors who did not appear to have prior experience in energy trading, the SPR office, prior to awarding contracts, had discussions with third-party companies involved with each offeror to ascertain whether the offerors had legitimate opportunities to move the SPR crude oil into the market. Only after the SPR contracting office was convinced that each offer represented a reasonable opportunity to meet the exchange objectives were contracts awarded.

On October 4, the Department announced that 11 companies had submitted the highest value exchange offers. By the end of five working days, eight of the 11 companies, representing 20 million of the 30 million barrels of crude oil offered, had submitted the necessary letters-of-credit.

Three companies requested a time extension to secure their letters-of-credit. The SPR contracting officer has the discretion to grant a time extension if it is determined to be in the best interest of the government. In all three cases, evidence was presented that serious negotiations were underway with reputable energy companies, and the contracting officer granted each of the three offerors a one-day extension.

Two of the offerors did not secure the necessary financial guarantees by the time the extension had expired, and the SPR office terminated both contracts. Both offerors agreed to a no-cost termination. The third company was able to arrange a transfer of title to the oil it had been awarded to another energy company which, in turn, supplied the necessary letter-of-credit. The successful completion of this transaction enabled the government to secure a favorable deal for the taxpayer and to move an additional 3 million barrels of SPR oil into the market with the necessary financial guarantees. It also enabled a small minority-owned business to be included in the pool of successful bidders.

Consequently, of the original 30 million barrels of Strategic Reserve offered for exchange, 23 million barrels are now under firm contract with financial assurances. In return, the Department will receive 23.8 million barrels for the Reserve during August-November of next year.

To put this exchange in perspective, it is important to note that the 23 million barrels of oil exceeds the 17 million barrels sold (from 34 million barrels offered) during the 1991 Desert Storm drawdown. Proceeds from that sale were deposited in a special Treasury account established for replenishing the Reserve, however because of budget constraints, it took until 1994 for the Reserve to be restocked. Under

the current SPR exchange, all of the crude oil plus a premium will be returned to the Reserve within a year after deliveries.

Deliveries of the crude oil have begun. Although the Department specified that crude oil was being offered for delivery during the month of November, we also indicated that earlier deliveries could be made if companies could make the necessary transportation arrangements.

Last Thursday, October 12, Morgan Stanley Dean Witter—one of the companies receiving an exchange contract—requested an early delivery of crude oil from the Reserve's Bryan Mound site near Freeport, Texas. Site operators were able to complete the necessary preparations, and 500,000 barrels of oil began moving into the Seaway interstate pipeline on October 13.

A second delivery of 250,000 barrels of oil is scheduled to begin moving today from the West Hackberry site in Louisiana at the request of Marathon Ashland Petroleum LLC, another of the successful offerors.

This shows, Mr. Chairman, that the Strategic Petroleum Reserve is capable of responding literally overnight to the need to move crude oil quickly into the nation's distribution system. We are especially proud of the operational personnel at our Reserve for their ability to respond quickly and efficiently in delivering crude oil to the market.

THE OCTOBER 16 SOLICITATION

Because two of the initial winning bidders could not secure the necessary letters-of-credit, seven million barrels of crude oil were offered for exchange on October 16 when the Department reissued its solicitation. Offers will be due on Monday, October 23, and deliveries will be scheduled for December with earlier deliveries again possible.

In addition to the amount of crude oil, the Department made the following changes to the solicitation:

- Companies must take delivery of crude oil from the Reserve before the end of December although earlier deliveries could be arranged. The original solicitation specified the month of November for oil deliveries from the Reserve.
- Given the concerns expressed by Members of Congress and others regarding the qualifications of the initial bidders, the Department decided to reinstitute a financial guaranty requirement for the bid. A bid bond must accompany all offers due on Monday. The bond must guarantee that, in the event the Department selects an offer but the offeror cannot produce the required letter-of-credit, the offeror must pay either 5 percent of the value of the offer or \$3 million whichever is less. This upfront requirement had been waived in the initial solicitation. To ensure that small businesses continue to have the opportunity to participate, the Department reduced the dollar threshold from \$10 million, the amount it would require in an actual emergency drawdown and sale of Reserve crude oil.
- The irrevocable letter of credit which the offeror must provide prior to actually acquiring crude oil from the Reserve is now set at 110% of the value of the Reserve crude oil on the day of the contract award (rather than the previous 100%). This will provide protection to the Government for the crude oil delivered from the Reserve plus the bonus percentage the offeror commits to return next year.

We continue to believe that the objective of moving oil quickly into the marketplace can be met by encouraging the widest range of possible qualified participants in the bidding process. We do not want to unfairly bias the bidding process against small or minority businesses.

THE HEATING OIL RESERVE

Although the Chairman's letter did not ask about the status of the Northeast Heating Oil Reserve, it is also a very important component of the Administration's energy preparedness efforts for this winter and has been established through the use of crude oil exchanges from the Strategic Petroleum Reserve.

On October 13, 2000, almost simultaneously with the first crude oil delivery out of the Strategic Reserve in Texas, the final shipment of heating oil was received for the government's reserve in the Northeast. The federal government now has a fully stocked, 2 million barrel inventory of emergency heating oil ready at three commercial terminals in the New Jersey and Connecticut as a supply cushion for consumers this winter.

To acquire the storage capacity for the heating oil for this winter, the Department is exchanging just over 117,000 barrels of Strategic Reserve crude oil. Another 2.7

million barrels of Strategic Reserve crude oil is being exchanged in return for the heating oil. The Importance of Reauthorizing EPCA

With the heating oil reserve now fully stocked, we urge Congress to complete legislation that would set an appropriate trigger for releasing the emergency supplies if necessary. The President can order the heating oil to be released under broad national authorities, but more regionally-specific authorities would be appropriate to address possibly supply problems in the Northeast this winter.

We continue to call on Congress to pass a renewal of the Energy Policy and Conservation Act with the inclusion of an appropriate regionally-specific trigger for the heating oil reserve. The Act provides direct authority that underpins the Department's full emergency oil response capability. There should be no ambiguity about the President's ability to use this important energy response tool.

EPCA reauthorization is also important because the Act provides limited antitrust protection for U.S. oil companies assisting us and the International Energy Agency plan for and respond to an oil emergency in a coordinated manner.

The House of Representatives has acted twice in the past several months to reauthorize the legislation, and hopefully, the Senate will take action before Congress adjourns.

This completes my prepared statement. I will be pleased to answer any questions Members may have.

Mr. BARTON. Thank you, Mr. Kripowicz.

We would now like to hear from Mr. Majak.

Your statement is in the record in its entirety, and we will give you such time as you may consume to elaborate on it.

STATEMENT OF HON. R. ROGER MAJAK

Mr. MAJAK. Thank you very much, Mr. Chairman, Mr. Boucher, members of the subcommittee. I am very glad to be here to discuss this morning the Commerce Department's authorities to regulate the export of crude oil and refined petroleum products.

At present, the Department imposes export controls on domestically produced crude oil on the basis of various statutory requirements that relate to its particular origin and mode of transportation. These requirements are set forth in statutes with which this committee is very familiar, including, of course, the Energy Policy and Conservation Act. With a few exceptions, most notably the Alaskan North Slope crude oil, which was freed for export in 1995, these statutes require an export license for domestic crude oil exports to all destinations, including Canada. The Commerce Department administers these export control provisions.

As I will discuss in more detail later, the administration also has discretionary authority under the Export Administration Act of 1979 to restrict exports of refined products. Those discretionary authorities have not been used since Malcolm Baldrige ended restrictions on refined petroleum product exports back in 1981, despite the fact that there have been some uncertainties in the oil market since that time.

There are only a few limited circumstances in which the Department will approve applications to export crude oil. These include exports from Alaska's Cook Inlet, exports to Canada for consumption or use therein, exports in connection with refining or exchange of Strategic Petroleum Reserve oil, and exports of California heavy crude oil, up to an average volume of 25,000 barrels per day.

During fiscal year 2000, the Department processed only 15 applications for the export of crude oil valued at \$858 million. Three of these licenses were for exports to Canada and the rest were for exports of California heavy crude oil, mostly for use as bunker fuel or to the Far East markets where environmental restrictions are

more liberal than they are here in the United States. Those licenses, by the way, are valid for a period of 90 days.

There is, of course, considerable interest regarding the scope of export controls that apply specifically to the Strategic Petroleum Reserve, the SPR. Therefore, let me address those controls in greater detail.

Applications for the export of crude oil from the SPR may be approved only if there will be a corresponding import of refined petroleum products that the Departments of Commerce and Energy determine are needed in the United States and we would not have been able to obtain those refined products without the export of crude from the SPR. This provision effectively blocks the export—or, so far, it has blocked the export of crude released from the SPR, unless there is a compelling national interest to permit it.

For example, if U.S. refineries are operating at full capacity and there is a need for additional refined product within the United States, it could serve our national interests to export SPR crude for refining and return to this country, or as a swap for already refined products. Although this is a useful option to have, to date we have not received any applications for the export of SPR crude.

Regarding the discretionary authorities I mentioned a moment ago to control refined petroleum product exports, the Export Administration Act of 1979 has a declaration of policy which states that controls may be imposed, quote, to restrict the export of goods where necessary to protect the domestic economy from the excessive drain of scarce materials and to reduce the serious inflationary impact of foreign demand, unquote.

To implement that policy, Section 7 of the Export Administration Act reads, in part, “the President may prohibit or curtail the export of any goods subject to the jurisdiction of the United States or exported by any person subject to the jurisdiction of the United States.” Those authorities, which would apply to refined petroleum products, have been delegated to the Secretary of Commerce.

Refined products, I should note, Mr. Chairman, derived from SPR crude oil, therefore, can be exported with no license required, except to a small group of embargoed countries, such as Cuba and Libya, unless we were to exercise the discretionary authority that I just described.

Mr. Chairman, some have suggested that the administration should consider imposing short supply export controls on home heating oil in order to ensure that adequate quantities will be available this winter. At this juncture, we believe that that would be a mistake for the following reasons:

First, over the past 2 months, U.S. refinery utilization rates have remained high, over 90 percent, essentially full capacity. They have declined slightly from about 96 percent to about 91 percent over the last couple of months, as demand decreased with the end of the summer driving season. Some of that capacity is off-line for maintenance, but we expect that high production margins will encourage refiners to defer maintenance where possible to keep maximum capacity on line. It would be unwise, in our view, at this point to impose regulations that discourage this so far orderly transition to maximum heating oil output. Oil and oil products are, of course,

fungible. An export ban on heating oil could encourage refiners to produce other products instead.

While we could impose a ban, a complete ban on the export of all refined petroleum products, we believe that would reduce the incentive for refiners to stay on line. A total ban would be a draconian measure that would likely cause greater market disruptions. For example, since the United States is, of course, a net oil importer, we are at risk of foreign retaliation if we were to impose a total ban on refined product exports.

Second, we do not project at this time that there will be a short supply of home heating oil this winter that the market cannot accommodate. As Energy's testimony indicates, the home heating oil reserve is already fully stocked, the conversion of refineries to heating oil production is proceeding smoothly, there is no shortage of feedstock. Although it is possible that some exporters will want to take advantage of higher prices that European consumers may be willing to pay, we cannot predict with any assurance the scope and impact of such export activity. Accordingly, we believe it would be unwise to impose burdensome and perhaps counterproductive new regulatory requirements based merely on the possibility of a shortage.

Under current law, Mr. Chairman, applications for the export of 250,000 barrels or more of any refined product in any physical year would require congressional review for a period of 30 days. Of course, if there were a total ban on exports, nobody would file for export applications, knowing that they would be denied. If, on the other hand, there were exceptions, the entire process would quickly become much more complicated and again, we believe, have unpredictable effects on oil markets.

In summary, Mr. Chairman, the Department is implementing crude oil short supply export controls that are required by statute. Discretionary quantitative restrictions on the export of refined products have not been imposed for almost 2 decades. While we will continue to monitor the situation closely in conjunction with the Energy Department, there appears to be no sound basis today to change course. Thank you.

[The prepared statement of Hon. R. Roger Majak follows:]

PREPARED STATEMENT OF HON. R. ROGER MAJAK, ASSISTANT SECRETARY OF
COMMERCE FOR EXPORT ADMINISTRATION

Good morning Mr. Chairman and Members of the Committee. I am pleased to be here today to discuss the Commerce Department's authorities to regulate the export of crude oil and refined petroleum products.

At present, the Department imposes export controls on domestically produced crude oil based on statutory requirements related to its origin and mode of transport. These requirements are set forth in statutes including the Mineral Leasing Act of 1920, the Outer Continental Shelf Lands Act, the Naval Petroleum Reserves Production Act, the Energy Policy and Conservation Act, the Trans Alaska Pipeline Authorization Act, and PL 104-58 "Exports of Alaskan North Slope Oil." With a few exceptions—most notably Alaskan North Slope (ANS) crude oil, which Congress freed for export in 1995—these statutes require an export license for domestic crude oil exports to all destinations including Canada. The Commerce Department administers these export control provisions.

As I will discuss in more detail later, the Administration also has discretionary authority under the Export Administration Act of 1979 to restrict exports of refined products (distillates). Those discretionary authorities have not been used since Malcolm Baldrige ended restrictions on refined petroleum product exports in 1981, despite periodic oil market uncertainties since then.

There are only a limited number of circumstances in which the Department will approve applications to export crude oil. These include exports from Alaska's Cook Inlet, exports to Canada for consumption or use therein, exports in connection with refining or exchange of strategic petroleum reserve oil, and exports of California heavy crude oil up to an average volume not to exceed 25 thousand barrels per day (MB/D).

At present, petroleum products (e.g., gasoline, kerosene, distillates, propane or butane gas, diesel fuel and residual fuel oil) refined within the United States are not subject to short supply export controls, with one exception. If the refined products were produced or derived from crude oil obtained from the Naval Petroleum Reserve (NPR) or became available as a result of an exchange of any NPR produced or derived commodities, a license is required to all destinations including Canada.

During FY 2000, the Department processed 15 applications for the export of crude oil valued at \$858,025,000. Three licenses were for exports to Canada and the rest were for exports of California heavy crude oil, mostly for use as bunker fuel or to Far East markets where environmental restrictions are more liberal than they are in the United States. Heavy California crude is of such poor quality that it is mainly used for asphalt production or mixed with residual fuel oil for bunker fuel for ships. Those licenses are valid for 90 days.

Applications for the export of domestically produced crude oil for consumption or use in Canada may be approved provided that none comes from a Naval Petroleum Reserve. Licenses are valid for one year.

There is, of course, considerable interest regarding the scope of export controls that apply to the Strategic Petroleum Reserve (SPR). Therefore, I will address these controls in greater detail.

Applications for the export of crude oil from the SPR may be approved only if there will be a corresponding import of refined petroleum products that the Departments of Commerce and Energy determine are needed in the United States and that we would not have been able to obtain these refined products without the export of crude from the SPR. This provision effectively blocks the export of crude released from the SPR unless there is a compelling national interest to permit it. For example, if U.S. refineries are operating at full capacity and there is a need for additional product within the United States (e.g., home heating oil), it could serve our national interest to export SPR crude for refining and return to this country, or as a swap for already refined product. Although this is a useful option to have, to date we have not received any applications for the export of SPR crude.

Our regulations also contain a License Exception that permits the export of foreign origin crude oil that is owned by a foreign government or its representative which is imported into the SPR for storage under an agreement with the United States Government. If the foreign oil has been commingled with domestic crude oil in the SPR, the export may only be permitted if the Energy Department certifies that the oil to be exported is the same quality and quantity that was imported into the United States. It is my understanding that at present, this is a moot issue since there is no foreign oil in the SPR.

As I have already noted, there are no short supply licensing requirements for refined petroleum products unless they are derived from Naval Petroleum Reserve crude oil feedstock. Refined products derived from SPR crude oil therefore could be exported with no license required, except to a small group of embargoed countries such as Cuba and Libya.

Regarding the discretionary authorities I mentioned earlier to control refined petroleum product exports, the Export Administration Act of 1979's "Declaration of Policy" states that controls may be imposed "to restrict the export of goods where necessary to protect the domestic economy from the excessive drain of scarce materials and to reduce the serious inflationary impact of foreign demand."

In order to implement this policy, the specific authority to prohibit or curtail the export of commodities determined to be in short supply (SS) is contained in Section 7 of the Export Administration Act of 1979 (EAA), which reads in part "the President may prohibit or curtail the export of any goods subject to the jurisdiction of the United States or exported by any person subject to the jurisdiction of the United States". These authorities have been delegated to the Secretary of Commerce.

Mr. Chairman, some have suggested that the Administration consider imposing short supply export controls on home heating oil in order to ensure that adequate quantities will be available this winter. At this juncture, I think that would be a mistake for the following reasons.

First, over the past two months, U.S. refiners utilization rates have declined from about 96% to about 91% of capacity, as demand has decreased as we moved away from the summer driving season. While some of that capacity is off-line for maintenance, we expect that high margins will encourage refiners to defer maintenance

where possible to keep capacity on-line. It would be unwise to impose regulations that discourage the orderly transition to maximum heating oil output. Oil and products are fungible. An export ban on heating oil would encourage refiners to produce other products.

While we could impose a ban on the export of all refined petroleum products, this reduces the incentive for refiners to stay on-line. This is surely a draconian measure that would likely cause even greater market disruptions. The United States is a major net oil importer. Discretionary actions taken by the Administration to restrict exports of U.S. petroleum products could result in retaliation, thus undermining the availability of crude oil supplies.

Second, we do not project at this time that there will be a short supply of home heating oil this winter. As Energy's testimony indicates, the home heating oil reserve is already fully stocked and production of distillates this year has been high. The conversion of refineries to heating oil production is proceeding smoothly. There is no shortage of feedstock. Although it is possible that some exporters will want to take advantage of higher prices that European consumers may be willing to pay, we cannot yet predict with assurance the scope and impact of such export activity. Accordingly, I think it is unwise to impose a new regulatory regime based merely on this possibility.

Applications for the export of 250 thousand barrels or more of any refined product in any fiscal year would require Congressional review—delaying action up to 30 days. Of course, if there were a total ban on exports, nobody would file for export applications knowing that they would be denied. If, on the other hand, there were exceptions, exemptions or other limitations, the entire process could quickly become very complicated and have unpredictable impacts on oil markets.

In summary, the Department is implementing crude oil short supply export controls that are required by statute. Discretionary quantitative restrictions on the export of refined products have not been imposed for almost two decades. While we will continue to monitor the situation closely in conjunction with the Energy Department, there appears to be no sound basis to change course now.

Mr. BARTON. Thank you.

The Chair would recognize himself for 10 minutes for questions, and then we will go to each member in turn for the 10-minute question period.

Mr. Kripowicz, how long have you been acting Assistant Secretary for Fossil Energy?

Mr. KRIPOWICZ. Since the beginning of September.

Mr. BARTON. Just this September, so less than a month and a half?

Mr. KRIPOWICZ. Yes, but I have been the principal deputy to the Assistant Secretary since 1995.

Mr. BARTON. Okay. Are you a political appointee or a career civil servant?

Mr. KRIPOWICZ. I am a career civil servant.

Mr. BARTON. A career civil servant. Is there a reason that we couldn't get a political appointee to come to this hearing today, that you are kind of the low man on the totem pole and you had to show up because you couldn't be at a meeting in Canada or taking your dog to see the veterinarian or something?

Mr. KRIPOWICZ. Sir, the Secretary is in Canada on diplomatic business, as you know, and the Under Secretary is appearing as we speak in the Senate, so we had a question of the two of us, which one would be able to do it, and so we—

Mr. BARTON. We are honored to have you. You probably know more than the other people that would have attended.

Mr. KRIPOWICZ. I would hesitate to say that.

Mr. BARTON. Some of our questions do deal with the politics of the issue, so it would have been nice to have a political appointee here.

When Chairman Bliley and I sent a letter to the Secretary and the President several weeks ago, we asked for any and all documents that relate to this policy decision that has been made. We received, exclusive of public reports, this pile of documents, which for a decision that is \$1 billion in magnitude is hardly a large number. We saw none from your office.

Mr. KRIPOWICZ. There are some documents in there generically from the Strategic Petroleum Reserve Office.

Mr. BARTON. Okay. Well, the transmittal letter says that other documents are forthcoming. I would assume, since you are the Acting Assistant Secretary for Fossil Energy, that this was a decision that the fossil energy group had something to say about. So would you do me a favor and when you go back check your files. Most of the documents that we have received so far are from the policy office. There appear to be no documents from your office. As a career civil servant, you probably keep pretty good files; and it would be very, very helpful to have documents that the people that actually know about the issue have helped prepare.

Mr. KRIPOWICZ. We will review our files again, sir. Most of the documents that come from fossil energy in this case would originate in the Strategic Petroleum Reserve Office, because they are the office that is responsible for it. So most of what I would have would be duplicates of whatever they have provided. But we are in the process of doing a check.

Mr. BARTON. Well, if you will just go back and look. You know, sometimes funny things happen.

Mr. KRIPOWICZ. Absolutely.

Mr. BARTON. Even the First Lady found documents up in a White House closet that she had not known about, so there is a possibility, if not a probability, that you might find some documents, too.

Mr. KRIPOWICZ. I have no closets.

Mr. BARTON. Okay.

Now, I want to talk a little bit about this issue of getting home heating oil. We have a document which we did get, if I can put this into the record, it is a memorandum dated September 6, it is from Melanie Kenderdine, who is the Director of Policy, on the issue of the SPR exchange, and I think we have copies to give. It is a September 6 document. We will get copies to the members and to you, sir.

[The information referred to follows:]

September 6, 2000

MEMORANDUM FOR THE SECRETARY

From: Melanie Kenderdine
Director of Policy

Subject: SPR Oil Exchange

ISSUE:

Can we structure an exchange of SPR oil to provide a premium for bids that convert crude oil to distillate?

BACKGROUND:

The authority to exchange oil from the Strategic Petroleum Reserve is designed to enable us to acquire additional oil for the Reserve. This is done through a so-called "time exchange" which takes advantage of a market condition known as "backwardation" in which current prices of crude oil are much higher than futures prices of crude. *Offering a premium to bidders to convert crude oil to heating oil does not enable DOE to acquire additional oil for the SPR and is therefore inconsistent with the exchange provisions in the statute.*

OPTIONAL METHODS OF EXCHANGE:

There are other options that would achieve an objective similar to that of offering a premium for conversion of crude oil to distillate.

- *Exchange crude oil for heating oil*

Under the terms of the statute we can exchange crude oil for heating oil. This is the type of exchange we employed in order to create the Home Heating Oil Reserve. We were however, *creating a government asset using our exchange authority and still retain ownership of the oil in the heating oil reserve.* Since heating oil has more value than crude, this type of exchange is consistent with the provisions of the statute that allow us to use a time exchange to acquire oil for the Reserve.

Limitations: this would only build the heating oil reserve, not put heating oil on the market, opening us up to accusations that we are competing with private industry for heating oil storage. There is little heating oil available right now; we might not find sufficient heating oil responsive to our solicitation. Even if we did, pulling heating oil off the market at the start of heating oil season would likely raise the price of heating oil.

- *Exchange crude oil for immediate delivery of heating oil and for crude at a later date*

This would involve a complicated two-step exchange. For example, we could exchange 30 million barrels of crude oil in October, and simultaneously re-exchange the heating oil for additional crude oil to be delivered to the Reserve in 2002. This would enable us to return 30 million-plus barrels of heating oil to the Reserve in 2002 (satisfying the statute requirements to use the exchange authority for oil acquisition) and put heating oil on the market in the interim.

Limitations: this is a very complicated and risky transaction. We would likely pay a premium for heating oil right now (most likely location for large additional volumes of heating oil appears to be Asia) and a two-step transaction, by definition, would cost more. This looks like market manipulation at the extreme. Also, such a large transaction with such specific terms would limit potential bidders to an extremely small group e.g. Exxon-Mobil, BP-Amoco, Shell, and few others. While such a transaction is arguably legal, Congress would likely have a very negative reaction as this appears to be abusing the intent of a time-exchange.

- *Exchange crude oil for crude oil*

This is the simplest way to encourage heating oil inventory production. When crude oil prices are steeply backwardated, as they are now, there is little incentive for refiners and marketers to hold heating oil inventory — they are fearful they will lose money when oil prices decline in the future. Putting oil on the market will temporarily lower the price of crude, thereby increasing refiner margins. *Any increase in refiner margins will encourage additional refining of crude oil to distillate.* Note: while refineries in the U.S. are at capacity and have limited ability to produce more heating oil, under normal conditions they would be cutting back runs now, after the peak gasoline season. The higher refiner margins that would result from more oil on the market would encourage refiners to keep refinery runs up to produce winter distillate.

Limitations: an SPR exchange of crude oil is a less-than-perfect way to increase heating oil inventories but our options are limited. An exchange of SPR oil would have the same effect as an OPEC increase in production — it would simply put more oil on the market.

RECOMMENDATION:

In the final analysis, the most reasonable alternative at this time is an exchange of crude oil for crude oil.

Mr. BARTON. It talks about the possible ways, and I won't put this in the record until everybody has had a chance to look at it, but it talks about possible ways to get additional home heating oil, and the subject is an SPR oil exchange. It talks about an exchange of crude oil for heating oil; it talks about an exchange of crude oil for immediate delivery of heating oil at a later date; and then it talks about an exchange of crude oil for crude oil, which is what ultimately happened. And the limitation on the crude oil exchange is, "an SPR exchange of crude oil is a less-than-perfect way to increase heating oil inventories, but our options are limited. An exchange of SPR oil would have the same effect as an OPEC increase in production. It simply puts more oil on the market. Recommendation." It says, "the most reasonable alternative at this time is an exchange of crude oil for crude oil."

Have you seen this document?

Mr. KRIPOWICZ. Yes, sir, I am familiar with it.

Mr. BARTON. Okay. Do you agree with the limitation that exchanging crude oil for crude oil simply puts more oil on the market?

Mr. KRIPOWICZ. It does not guarantee that you get heating oil into the Northeast, that is correct, sir, but our analysis is that from 3 to 5 million barrels out of this—

Mr. BARTON. I am glad you mentioned that number. Let's talk about that a little bit. Let's put this chart up.

The gentleman who heads the EIA office, Mr. Mazur, who has been before our subcommittee, and I am sure you know him, he is a reputable man.

Mr. KRIPOWICZ. Yes, I do.

Mr. BARTON. He issued, or his office issued a statement last week that says, of this 30 million barrel release, only about 10 million barrels is actually going to be added to the U.S. supply. That 20 million barrels is going to displace oil that would have been imported.

Do you agree or disagree with that?

Mr. KRIPOWICZ. That is what the analysis was based on.

Mr. BARTON. Okay. So if we look at this little chart over here, it says, how much heating oil will we get? Although there is 30 million being released, 20 of that 30 million, according to EIA, just displaces imports, so in that blank would you say we could agree to put in 10 million barrels?

Mr. KRIPOWICZ. Well, the refineries will actually receive 30 million barrels of crude oil from the Reserve.

Mr. BARTON. No, no. Now we are talking about additional oil. Had there not been an SPR release, you know, according to EIA, there would have been 20 million barrels of oil imported. EIA says this release actually results in 10 million additional barrels.

Mr. KRIPOWICZ. That is correct.

Mr. BARTON. So could we put a 10 there? U.S. refineries will receive 10 million additional barrels of crude oil? Do you agree with that?

Mr. KRIPOWICZ. Yes, sir.

Mr. BARTON. Okay. Now, let's see, how much of that will be processed into middle distillate? Now, according to the averages that we have seen and that you yourself alluded to in our briefing a

month ago, you said that between 22 to 25 percent of a barrel of oil normally goes into middle distillate. Do you agree? What is your number today?

Mr. KRIPOWICZ. It is approximately 25 percent, sir.

Mr. BARTON. All right. So let's put 25 percent. Give you the high range of that.

Now, according again to the public documents that we have received, in middle distillate, about 70 percent goes into highway diesel, about 20 percent goes to industrial uses, and the number that we show is 10 percent goes to home heating oil.

Now, what are your numbers? Those are industry averages from EIA public documents that, of the 25 percent that goes to middle distillate, you get about 70 percent into highway or diesel fuel, about 20 percent into industrial use, and about 10 percent into home heating oil. Do you want to give us different numbers, or can we use those numbers?

Mr. KRIPOWICZ. You can use those numbers, if I can qualify that in some fashion.

Mr. BARTON. You can qualify all you want.

Mr. KRIPOWICZ. It would result in that amount of oil that could only be used for home heating oil purposes. The amount of barrels that go to highway diesel are interchangeable with the barrels that would go to heating oil, so if the demand is for heating oil, then you would be able to use some of the highway diesel fuels for home heating oil. So although on a nominal basis those numbers are correct, those two fuels are fungible going in the heating oil direction but not coming back the other way.

Mr. BARTON. I actually understand what you said. I won't disagree on technical merit with what you said.

Well, but for purposes of the hearing today, let's put 10 percent in home heating oil and 70 percent into highway diesel, and 20 percent into industrial. Now, if you do the math on that, 10 percent of 25 percent of 10 million is 250,000 barrels.

Mr. KRIPOWICZ. That is the minimum. That is correct.

Mr. BARTON. Now, how does that square with the continued trumpeting of 3 to 5 million barrels of additional home heating oil? Those are EIA numbers, and those are administration projections and industry averages, and according to our basic Aggie math here, we get 250,000 additional barrels of home heating oil. We have a discrepancy of about 3,000 percent—250,000 goes into 3 million about 12 times, I think.

Do you want to educate the subcommittee on Clinton-Gore math that goes from 250,000 to 3 million?

Mr. KRIPOWICZ. My reaction is that the 25 percent gives you approximately 2.5 million barrels which can be used for heating oil. And it is new barrels that would displace other barrels that might have gone for other purposes.

Mr. BARTON. But you and I both know—I agree with what you said in your qualification that the diesel highway fuel is fungible. It is not quite interchangeable, but you can certainly burn it in a boiler or a burner for home heating if you needed to. But if you take that away from the diesel fuel market, you and I both know there is going to be heck to pay in that market.

Mr. KRIPOWICZ. That assumes that the market was expecting this additional 70 percent. If the heating oil market is the market that requires the oil or the product—

Mr. BARTON. This subcommittee would really like a justification of how you get the 3 to 5 million barrel number based on your own numbers that say you are only going to have an additional 10 million barrels come on to the market, and if you go through the normal refinery process, giving you the benefit of the doubt on what will be processed into a middle distillate. But 25 percent is the high end, not the average. The numbers don't square. They don't square in terms of what is really happening in the market. They may square in terms of what gives you the greatest political impact.

Again, that's why you are not the best witness to be here because to your credit, sir, in all my dealings with you, you have never been political. You've been a straight shooter. These are the facts. So don't take it personally, but send back up the food chain at DOE that the people that made the decision in my opinion made it for political purposes and the numbers just do not back it up.

Now let me ask a question about refinery capacity. In our briefing before the hearing that we had about a month ago refineries were running about 95 percent, and we were told that the Department of Energy was going to be engaged in discussions with them, and because the refinery margins were high that you could either get them to maintain their capacity at 95 percent or maybe even increase it a little bit. Now, it appears that they have gone down to about 91 percent.

What has happened to cause them to go down rather than to stay at the higher level they were at at that time? Was it the routine maintenance that they have to do?

Mr. KRIPOWICZ. Yes, sir.

Mr. BARTON. Okay. Now, if, in fact, refinery operations have declined by 5 percent, how do you get more fuel oil refined when their capacity is going down?

Mr. KRIPOWICZ. Well, sir, they are maximizing distillate right now and actually this past week the production of distillate went up even though the refinery utilization went down. It went up by 140,000 barrels.

Mr. BARTON. So what have they changed if their capacity of production has gone down? Are they somehow magically being able to get 30 percent of the barrel into the middle distillate.

Mr. KRIPOWICZ. They are maximizing that fraction. I don't know how high an individual refinery can go.

But the second point I would like to make is that it is projected that beginning in November that these outages will drop considerably and there should be more than enough refinery capacity available to produce the extra oil.

Mr. BARTON. Well, I have gone way over my time. I got carried away. I apologize. I recognize the gentleman from Virginia for 10 minutes.

Mr. BOUCHER. Thank you very much, Mr. Chairman. I want to join with you in welcoming these two distinguished witnesses to the subcommittee this morning. Mr. Kripowicz, in particular I want to thank you for your presence here and in participating in this conversation. I noted with interest in Mr. Majak's statement that

there have been no restrictions placed on crude oil exports since the time of the Reagan Administration. And if that was an accurate statement, it would appear that in 1991 when the SPR was drawn down during a time when the Nation was at war, there were no restrictions placed on exports at that time.

Is that correct, Mr. Majak?

Mr. MAJAK. I made that statement with respect to controls on refined products only, not with respect to crude.

Mr. BOUCHER. So on refined products there have been no restrictions on exports since the years of the Reagan Administration.

Mr. MAJAK. That's correct.

Mr. BOUCHER. So there were no restrictions imposed in 1991 when the SPR was drawn down at a time when the Nation was at war?

Mr. MAJAK. Not with respect to refined products.

Mr. BOUCHER. Not with respect to refined products. It seems to me there is little difference between that circumstance and what we confront today, and I would simply note that it seems somewhat inappropriate that those who are arguing that somehow your policy is shortsighted for not having imposed restrictions on the export of refined products now take no note of the fact that during 1991 the exact same circumstance existed and, once again, no restrictions on exports were imposed. I won't even ask you to comment on that. I will simply note it in passing.

Mr. Kripowicz, Congress has failed to reauthorize the Energy Policy and Conservation Act, and that is a condition that concerns me greatly because your existing authority to manage the SPR is based on language that is contained in an appropriations bill and it is somewhat limited. And I am troubled that going into this winter at a time when there is instability in the Middle East and when there may be a real need to draw down the SPR in order to deal with supply disruptions we don't have the authority to do that.

I would simply ask you if you share that concern and if you have any comment about that condition.

Mr. KRIPOWICZ. Sir, it is mentioned in my statement that we feel that the passage of the Energy Policy and Conservation Act is essential. There are a couple of authorities that are important, one regarding the Northeast heating oil reserve in particular that we do not have in place; a regional trigger for the use of that reserve should it become necessary. Second we must restore the ability of our oil companies to participate with the International Energy Agency—if a consultation was necessary because of an emergency supply situation in oil. So those two things are particularly important to the passage of the act.

Mr. BOUCHER. And you would agree that it is in the national interest to have EPCA reauthorized and signed into law as soon as possible?

Mr. KRIPOWICZ. Yes, sir, and we have said that many times. And I would note the House has passed it twice.

Mr. BOUCHER. Certainly with the bipartisan support of members of this committee.

Mr. Kripowicz, I think it is fair to say that one of the most popular and broadly supported steps that your office has taken on a

bipartisan basis has been the establishment of the Northeastern reserve.

Mr. BOUCHER. I want to commend our colleague, Mr. Markey, who is with us today, for the leadership that he exercised in raising the concept of creating this Northeastern reserve, which is so necessary to assure stability in the market there for home heating oil.

I would simply ask you a couple of questions about the current status of the reserve. First of all, is it ready to be deployed? Where does it stand today? Second, how do you envision this particular reserve helping consumers of home heating oil in the Northeast during the course of this winter? And third, what actions, if any, should we take here in the Congress in order perhaps to give even greater legal foundation to the Northeast heating oil reserve.

Mr. KRIPOWICZ. First, Mr. Boucher, the reserve is full as of last Friday. So we have the full 2 million barrels, a million barrels in New York Harbor and a million barrels in Connecticut. Also, we have issued today draft procedures for the sale of the oil should it become necessary to release oil from the reserve. We think it is very important that one thing that Congress could do for us is give us a regional trigger, which would make it not necessary for the President, who under current circumstances would have to declare a national emergency under the Strategic Petroleum Reserve authorities, and right now that would be very much more difficult than it would be if we had a trigger, which is included in the pending legislation.

Mr. BOUCHER. All right. Thank you. I will ask one additional question and that relates to the newspaper articles that have been published that suggest that the Department of Energy did not know very much about the bidders in this most recent drawdown of the SPR, and my question to you is why you chose to proceed as you did. It appears to me that you had two choices in terms of making sure that the people who were successful in bidding and who eventually would have contracts for the distribution of this oil had the financial ability to perform their obligations. You could have had a prequalification process as a consequence of which a bond would have been posted in advance, and that would have been before the bids took place, or you could have chosen to do as you did and simply allow the bids to occur but then require that letters of credit be produced by the successful bidders before they were permitted to come into the possession of the oil.

Tell us why you chose to proceed as you did. I am sure there was a reason for that, perhaps based on the need to get the oil into the market quickly, and perhaps a delay would have been created had you undertaken the prequalification process. But I would like to hear your statement as to why you proceeded that particular way.

Mr. KRIPOWICZ. We believed that speed was of the essence, so that was one of the factors. The second thing was to get the widest number of bidders and have the greatest chance of being able to release the 30 million barrels in the timeframe allotted. We have used exchanges before, and in those exchanges we have not had bid bonds included. So we felt that standard procedure would probably work. Bid bonds are expensive also, and we would have gotten less of an exchange ratio because people would have to take into account the expense of the bond. And I would want to emphasize

here that there was also no up front risk to the government because nobody gets any oil unless they come up with the letter of credit after 5 days.

I would also point out that in the process, we obviously looked at the three people that we did not know anything about and we talked to them, we got whatever public information was available. We got certifications of their financial responsibility and other fiduciary certifications, and we had evidence from major people in the oil industry that they were seriously discussing trading this oil with them, and that is why we went ahead with those three.

Mr. BOUCHER. And at the end of the day employing the process that you chose to employ, there was no risk to the government that any of this oil would be lost or that the government would not receive full payment for it; am I correct in saying that?

Mr. KRIPOWICZ. Absolutely. We did not get the letters of credit, so we did not release the additional 7 million barrels.

Mr. BOUCHER. Thank you, Mr. Kripowicz. Thank you, Mr. Chairman.

Mr. BURR [presiding]. The gentleman's time has expired. The Chair at this time will recognize the gentleman from Illinois, Mr. Shimkus, for questioning.

Mr. SHIMKUS. Thank you, Mr. Chairman. I will probably follow the line of questions of the gentleman from Virginia. But first, I don't want to continue to sound like a broken record. Congressman Knollenberg talked uranium reprocessing, a national energy strategy using all our energy resources. And if the chairman would allow me to deface his poster a little bit, if my staffer, Mr. Fitzgerald, would place a little—put it on the arrow, B-20, which is biodiesel, which has been allowed in the Energy Policy Act we had inserted, myself and Karen McCarthy, through this committee using a renewable fuel standard, 20 would represent—yes, put it on the other one, too—would be 20 percent soy or beef tallow or whatever, 20 percent of the gallon could be replaced with diesel which would affect again—this is all part of the energy portfolio, having a renewable portion, having uranium. We will take that off in a minute, Mr. Chairman. I know you may not appreciate that. So I make the case again for the renewable fuels, and I just wanted to use that chart.

Mr. Kripowicz, I wanted to talk about this no possibility of loss for a second. We have these bidders. They establish a line of credit. They get delivery. They default. They go bankrupt. We get the letter of credit. The barrel price doubles. The amount of the barrels of oil that we can buy per the letter of credit has now been reduced by one-half, wouldn't you agree?

Mr. KRIPOWICZ. In that circumstance we probably wouldn't buy the oil at that point. We can hold on to the funds from the letter of credit until such time as we get a reasonable amount of oil in return. If the price was double what it is now, we certainly probably would be doing several other things with the Strategic Petroleum Reserve anyway.

Mr. SHIMKUS. But the argument is sound that if the price goes up and we have to call in the letter of credit, we may—we may not—and if we did go buy, we may not get even the additional

amount that was projected by the DOE in this legal swap scheme that we have actually developed to put oil into the market.

Mr. KRIPOWICZ. If the contractor defaulted. If the contractor does not default, the contract calls for the amount of oil and not based on current price.

Mr. SHIMKUS. Correct. We have a letter of credit.

Mr. BARTON. Will the gentleman yield?

Mr. SHIMKUS. I will.

Mr. BARTON. I think this is an important point. This so-called swap works if the futures market at the time of the swap is right and oil prices are lower next summer. Then there is more oil available and the people that got the oil will replace it. They can make a little money and then give the Strategic Petroleum Reserve more oil than was in the reserve when they took it out. But if the futures market is wrong and prices go up like the gentleman from Illinois is saying, then it doesn't work.

So if I understood what you just told him and what you told us at the briefing a month ago, you just extend the contract. You do not actually call it in. You just give them more time and you hope eventually that the market goes back down.

Mr. KRIPOWICZ. It would not be in the best interest of these contractors, other government contractors, to be part of the oil business and to default on a large contract to the government because the price isn't correct.

Mr. BARTON. I don't want to take too much of your time. We will come back to that.

Mr. SHIMKUS. That is fine. But it is interesting when we bidders who—you know, I really have great respect for Congressman Hinojosa and his story about small business. I support small business totally. But his statement mentioned he had a factory, he had employees. He had means to try to comply with government contracts. Here we have a son and a mother in an apartment in Harlem with no means of production, transportation, distribution. So I, again, with all due respect to my colleague from Texas who testified earlier, this is apples and oranges. It is two difference processes.

Let me ask a question on one thing that hasn't arisen in this debate. Although we have heard the terms now in a couple hearings, we are at refinery capacity between 90 and 96 percent. And in the briefings we had, both in the hearing publically and some of the private briefings, we talked about how they need the time for the refineries to retool, change, and of course that usually happens at certain times of the year. And based upon that, there is a debate out in the country that because we have not increased refinery capacity there may be an attempt to even more isolate the United States as refineries are moved offshore and as we start importing the finished product instead of refining it here in the United States. Can you speak to that concern?

Mr. KRIPOWICZ. I know that the number of refineries has decreased considerably over the past 10 to 15 years, but the refining capacity has actually stayed steady or slightly increased, and we expect that capacity to increase further.

Mr. SHIMKUS. But demand has also increased across the board?

Mr. KRIPOWICZ. When demand increases, then there will end up being more imports if we don't increase—

Mr. SHIMKUS. And you are saying imports are refined products.

Mr. KRIPOWICZ. If we end up using refined products, so that is correct.

Mr. SHIMKUS. So if the administration has a concern about obviously a refined product, as home heating oil is, and we have not moved in the direction of increasing refinery capacity by known plants in the Nation, do you not think that it would probably be in the Nation's best interest across the board in energy needs to have a policy that would help our country continue a refinery base in this Nation?

Mr. KRIPOWICZ. Absolutely.

Mr. SHIMKUS. Thank you very much. The last thing that I want to ask, and I think this goes to Mr. Majak. I can find my scribbled notes. We belong to the International Energy Agency. Would you be the one who addresses that?

Mr. MAJAK. I believe we are a member, but I am not—

Mr. SHIMKUS. Mr. Kripowicz?

Mr. KRIPOWICZ. We are a member, yes.

Mr. SHIMKUS. Because we are a member of the International Energy Agency we have some requirements to meet as far as the availability of natural—or actually reserve of fuel based upon being a member of that; is that correct?

Mr. KRIPOWICZ. That is correct.

Mr. SHIMKUS. Do you know how many days on hand we are required to meet the requirements of being part of that group?

Mr. KRIPOWICZ. 90-day supply of crude oil.

Mr. SHIMKUS. How many barrels do we have—actually even before we did the SPR release, how many barrels did we have on hand?

Mr. KRIPOWICZ. I will give you an approximation. It is roughly 57 days worth.

Mr. SHIMKUS. 570 million?

Mr. KRIPOWICZ. That is in the Strategic Reserve. The 90-day supply requirement also includes private stocks, and we are in the neighborhood of 120 days, as I recall.

Mr. SHIMKUS. So your position is that we meet that standard?

Mr. KRIPOWICZ. Yes, we do.

Mr. SHIMKUS. And that is good for clarification because obviously if it was just dependent upon the SPR, which would be about 57 days, we would not.

Mr. KRIPOWICZ. That is correct.

Mr. SHIMKUS. And as we would deplete oil from the SPR, we would be even more out of whack. But I will thank you for your comments. That is why we have hearings, so we can clarify some of these issues. I didn't know that we should include corporate holdings of oil reserves. And with that, Mr. Chairman, I will yield back my time.

Thank you for answering the questions.

Mr. BARTON. The gentleman from Massachusetts is recognized for 10 minutes.

Mr. MARKEY. I thank the chairman very much.

So let's talk about the emergency situation that we have here today and this emergency hearing that we have had to call on short notice. What is the emergency exactly? The emergency is that oil prices have climbed to nearly \$40 a barrel about a month ago. The President ordered the Strategic Petroleum Reserve to be deployed. Oil prices dropped substantially, down to \$32 or \$33 a barrel. It affected the refined product price for home heating oil, gasoline. They both dropped.

What is the problem? What are we investigating here today? The problem from the Republican side is that the price has dropped. This is an emergency on their side. This is terrible. What's going on? People are paying lower for home heating oil, lower for gasoline all across the country even though they predicted there would be an emergency. So we must investigate and find out what went wrong with the free market control by oil company executives in Texas, Louisiana, Oklahoma, and over at OPEC. This is screwing up their profit taking for the rest of the winter all across the country. We had planned on having all these revenues from the rest of country pouring into their States, and we need a hearing on it and we are having it right now.

Now because they just can't have a hearing on that, they have to investigate whether or not a young black guy living in a home with his mother up in Harlem has applied for the ability to be able to contract on this fuel. Now, ladies and gentlemen, he applied, he was denied. He couldn't find financing. However, let me ask this. If BP Amoco had applied and couldn't find the financing, would we be having a hearing right now? No. But if BP, black person, applies and can't find the financing, now we have a hearing. A black person can't find financing or if a young man in Texas who had a mother and father living in a hotel room in Houston wanted to startup an oil company, George W. Bush, and had no other previous business experience and was able to find financing and was able to find it, would we have a hearing just because he had a mother and father living in a hotel in Houston? No. We would say, look, he has a fine background. Look at his mother and father. Look at the fine record they have. They went to fine schools. But if we find a young man whose mother never went to college living in Harlem who wants to get into the same oil market, well, that is a scandal.

What went wrong? Even though the Department of Energy rejected the contract because he couldn't find the financing, there should be a hearing. Why couldn't he find the financing, not that he couldn't and it was rejected by the Department of Energy, and that they acted upon sound principles of not having the U.S. Government be the bank. But this certainly doesn't merit a hearing.

Now we call it social engineering. And the gentleman from Illinois puts up his B-20 over here. Soy.

Mr. SHIMKUS. Soy.

Mr. MARKEY. Soy and beef tallow I think it is. I don't know what that is exactly up in Boston.

Mr. SHIMKUS. Fat.

Mr. MARKEY. But we are to be making oil out of it. Now I know we are going to do that because we want farmers to stay on the farms because that is good social policy and we do not want these

hard working farmers to have to leave after hundreds of years of farming that same land because that would be bad for the country if these farmers actually had to go into the city and take jobs. So we create a social policy that we are going to make oil out of beef tallow.

Now, I will go along with it. I don't know what it is exactly. And the gentleman has convinced me it is good social policy to keep these farmers there. We do not want the sons and daughters leaving the farm and going to the city, even though we don't need them on the farm anymore, because it is good social policy. It keeps some stability out there in rural America. That is okay. And God knows we wouldn't want to take away the oil depletion allowances or stripper well benefits because that would be—I guess that is social policy, isn't it, because we want those stripper well wildcatters to have those extra benefits. We wouldn't have to actually have to compete against big companies. But if a black person wants to do it, that is wrong. We got to have an emergency hearing. That is a scandal, even though the Department of Energy said he could not come up with the financing.

Now, I appreciate the fact that you are having this hearing, concerned now after the oil has been released that there may not be as much home heating oil to help us in the Northeast as you would like now that it has been released. I appreciate that. Now, you would think that we would be the ones that would be more concerned about that than you, Mr. Chairman. But to tell you the truth, we have got a pretty high confidence level that this is all working right now. Mr. Kripowicz made it quite clear that a lot of these fuels are now interchangeable and that, if not the market, then I think some bully pulpit lecturing from whoever might be President later on this winter might be able to ensure that with that additional supply of oil, that the home heating oil needs of the entire Northeast, parts of the Midwest could be met.

So I don't know why we are having this hearing. Well, let me put it like this. I know why we are having this hearing, but we should not be having this hearing. The deployment of Strategic Petroleum Reserve worked, prices have dropped. There is no scandal when a young black man seeks to go into the oil industry almost dominated exclusively by white men.

Mr. BARTON. Would the gentleman yield?

Mr. MARKEY. It is not a scandal that the marketplace is beginning to deal with this new in-flow of oil in a way which is going to provide—

Mr. BARTON. Will the gentleman yield?

Mr. MARKEY. I will be glad to.

Mr. BARTON. I will be glad to give you additional time.

Until we had the hearing I wasn't aware of the race of any of the potential bidders. You have repeatedly, and Mr. Wynn before you, have repeatedly attempted to racially polarize a policy hearing on the use of the Strategic Petroleum Reserve. But I am not aware of anybody on this side of the aisle that has raised any objection about potential bidders based on their race. Now if you've got anything that I as subcommittee chairman have put out based on that, because I wasn't aware of that.

Mr. MARKEY. Mr. Chairman, if I may reclaim my time, on October 17, which I think was yesterday, I may be wrong, you sent to my office and every one of our offices your subcommittee briefing memo, which includes an attached story from the Wall Street Journal talking about black entrepreneurs who are unknowns.

Mr. BARTON. It is the Wall Street Journal you have got the problem with.

Mr. MARKEY. No. You attached a three-page, four-page Wall Street Journal story to your memo to us. You gave it to us as the basis for the material that was going to be covered in this hearing. You did that.

Mr. BARTON. If the Wall Street Journal is raising concerns about race, that is their problem. That is not my problem.

Mr. MARKEY. That is what the story in the Wall Street Journal is about. It is about the black entrepreneur. You sent it to us.

Mr. BARTON. Take your concerns up with the Wall Street Journal.

Mr. MARKEY. I am taking my concerns up with whoever attached it to the memo from your staff to every other staff on the Hill and to all of the people who are sitting out here. This is a hearing, as far as the people who have this memo are concerned, about that black entrepreneur.

Mr. BARTON. Well, I am not asking any questions—I wish we had more entrepreneurs of all colors. I do find it somewhat ironic that DOE opened the bidding to anybody in the world who had the sense enough to read about it. I quite frankly wish that some of us had gone together. I wouldn't mind making an extra million dollars just by bidding and getting a letter of credit and flipping it. It is probably illegal for us to do that because of the positions we hold.

I will yield back, and we will give you additional time.

Mr. MARKEY. Again, I thank the gentleman. And I don't mean to say anything other than the fact that it is obviously meant to be one of the subjects for today's hearing. But you now, at the end of the day for better or worse, this is a political hearing. Okay. Now, obviously that is why you are requesting that the political appointees from the Clinton Administration be here today. It is not quite as edifying a hearing to have the technical people from the Department explain to you exactly why all of this is working. But at the end of the day we should not be, in my opinion, doing anything other than praising what has happened over the last month. It is great for consumers. It is great for drivers all across the country. And the prospects are that it is going to get better as the winter goes on and if we allow them to implement it. And we shouldn't try to stigmatize one young black man, who is trying his best to crack into what has been an exclusive club historically. Even though he was unsuccessful I think, it is a worthy attempt and maybe in years ahead somebody will be successful and they can crack through.

There were a lot of people before Jackie Robinson, there were a lot of people before Colin Powell who tried to reach the upper levels of other industries, other professions. And who knows, maybe we will some day come back and we will have him here as an expert

witness talking about how he has overhauled some part of the energy industry.

I don't think we should have an extended discussion. You didn't do it, Mr. Chairman, but other members of the committee did have an extended discussion about the worthiness of people from minority groups being in this business. I thank you.

Mr. BARTON. I took some of your time, so if you—

Mr. MARKEY. No.

Mr. BARTON. The gentleman from Oklahoma, Mr. Largent, is recognized for 10 minutes.

Mr. LARGENT. Thank you. For those of you that got the opportunity to hear that diatribe from my friend from Massachusetts you heard an angry, frustrated, bitter Red Sox fan.

Mr. BARTON. Excuse me.

Mr. LARGENT. He hates to see the Yankees in the World Series again. He is taking it out on all of us.

Mr. MARKEY. Will the gentleman yield? This is without question 1 week where it is an insult to call me a Yankee.

Mr. LARGENT. Did the chairman have something?

Mr. BARTON. I was really supposed to recognize Mr. Burr in order and I skipped over him, but we recognize you, Mr. Largent. So I will give you your 10 minutes, and then we will go to Mr. Burr.

Mr. LARGENT. I won't take 10 minutes. Mr. Majak, in your opening testimony you talked about export controls for limiting the ability of people to export any of the petroleum that is released from the Strategic Petroleum Reserve; is that correct?

Mr. MAJAK. That is correct.

Mr. LARGENT. Was that to make us feel good that this would not be exported?

Mr. MAJAK. An export license is required for such exports and we have not received any applications; therefore, we would believe that none has been exported.

Mr. LARGENT. Okay, but I guess the question I have for you, because we have some international oil companies in Tulsa, Oklahoma and I have friends that work there, and I know for a fact—I mean, that we get into this word that I didn't know until I got into Congress. We talk about fungibility. What prevents a company that is doing business both in the United States and Europe, for example, where prices of home heating oil and fuel is astronomically higher than it is here, what prevents a company that is doing business all over the world from simply purchasing some of the SPR release for its domestic purposes and basically shifting that in a paper shift to selling additional barrels of oil overseas?

Mr. MAJAK. Well, in the export control area, substitution is admittedly a problem. We depend upon the voluntary compliance of companies not to engage in substitution, which would evade the restrictions on the direct export of oil and other products that we control. But as a practical matter your point is a good one. It is difficult to assure that no substitution takes place.

Mr. LARGENT. In reality it is not even illegal?

Mr. MAJAK. It is addressed in some of the legislation, particularly with respect to the Naval Petroleum Reserve. It is not addressed in other of the legislation that applies here.

Mr. LARGENT. The truth is it is good practice. I mean, if you are out to make the greatest return for your investors and you can get more for your oil in Europe today than you can in the United States and you have the opportunity of having additional petroleum products put on the market in the United States and you just substitute and shift your emphasis to Europe, you are going to get a higher return on your dollar, and the truth is that in fact has been the net result of the release of 30 million barrels of oil from the Strategic Petroleum Reserve. That is going on. Is that not so?

Mr. MAJAK. I—

Mr. LARGENT. You don't have to answer. I know it is so. Do you know it is so?

Mr. MAJAK. I don't know it is so. As far as whether it is good business or not, it may be, provided it is not an intentional effort to evade the national security export controls legislated by Congress.

Mr. LARGENT. Mr. Kripowicz, I have a question for you. I was listening to Mr. Markey talk about these entrepreneurs and so forth, and I guess the question I have is if the goal is to lower the price of fuel oil for his constituents in Boston, how in effect are we doing that if we are allowing middle men, call them entrepreneurs, middle men to profiteer as a result of going through this bidding process? And I don't know if the numbers were correct or not but some were talking about profiting like \$6 million simply by taking the oil from DOE and turning it over to Amerada Hess, somebody like that. Somebody pays that \$6 million, and it is the consumer. So how do we in effect lower the price if we are allowing these middle men who have no previous experience in the oil and gas industry to take that \$6 million bite out of the price of fuel oil? How does that work? Is that good public policy?

Mr. KRIPOWICZ. First of all, I wouldn't imagine that there was \$6 million of profit involved in this. But second, that is the role of traders. These people were acting as traders. There are large traders as well as small traders in the oil business all the time. They do a lot of the buying and selling and trading of oil and product. And that is the way the market works and you can't take these people out of the market.

Mr. LARGENT. You were not going to approve them until they got a line of credit from a credible oil and gas company.

Mr. KRIPOWICZ. The line of credit is from a financial institution, even the oil and gas companies have to get a line of credit from an independent financial institution.

Mr. LARGENT. Well, all of the financial institutions that were seeking relationships with these men were oil and gas companies, according to the story. Again I am going by what is on here.

Mr. KRIPOWICZ. The relationship they were seeking was to take over the contracts, I would expect, or else to process the fuel—

Mr. BARTON. Would the gentleman yield?

Mr. LARGENT. I will yield in just a second, Mr. Chairman.

I will say just again, I don't believe, after working here for 6 years, I don't believe everything I read in the paper, that is for sure, any paper. But here it says, Mr. Stroud won't discuss which companies were vying for his oil but at one point he thought he had an offer to buy him out for \$1.50 a barrel, or \$6 million. That is

just one of the three individuals that this story highlights. So that is where I got my figures. I just wanted you to know that.

I yield to the chairman.

Mr. BARTON. If the bidder for the oil had offered to pay cash for it, would that have been accepted? Is that allowed or did they have to agree to this?

Mr. KRIPOWICZ. This was not a sale.

Mr. BARTON. You couldn't let them pay cash?

Mr. KRIPOWICZ. That is correct.

Mr. BARTON. That is why the letter of credit was necessary. There had to be some security on the off chance that they were not on the up and up or the market changed, that there would be some guarantee to the government they would get something back.

Mr. KRIPOWICZ. And because it was not a sale but an exchange, what we were asking in payment in essence is more oil, not cash.

Mr. BARTON. What if they had put more oil up right then? That doesn't make sense, but what if they said you give us 7 million, we will give you 8 million barrels right now? Would that have been allowed? There is no reason for them to do it but would it have been allowed?

Mr. KRIPOWICZ. I don't believe under the procurement that would be allowed.

Mr. BARTON. You would force them to take the oil?

Mr. KRIPOWICZ. And not give it back to us—

Mr. BARTON. Until next year. Okay.

Mr. LARGENT. Mr. Chairman, I want to conclude by saying that I know that many members of committee feel like that this is a politically motivated hearing, and perhaps it is. But I would say that I do think this is an important issue and I think it is something that we need to deal with when we come back in the 107th Congress. And that is to define and be able to put some parameters about why we need a Strategic Petroleum Reserve, and I think we do, and what those instances are that would precipitate release from the Strategic Petroleum Reserve.

I think we talked about having a national energy policy. I think part of that national energy policy has to include a sound and reasonable policy on the use of the Strategic Petroleum Reserve. It shouldn't be used to balance the budget, and Republicans tried to do that. It shouldn't be used for political purposes.

And I would say finally that the government should not be in the position of manipulating prices of anything, oil, corn, wheat, any of that. That is not the responsibility of the Federal Government to ensure that we have lower prices or higher prices for any commodity.

And with that, Mr. Chairman, I yield back my time.

Mr. BARTON. I thank the gentleman from Oklahoma.

The gentleman from North Carolina, who has been very patient, is recognized for 10 minutes.

Mr. BURR. Thank you. I regret that Mr. Markey chose to leave. It was apparent that he did visit the Boston debate. It was not apparent to me until the sigh came into the microphone, but clearly he learned something at that. It is indeed troubling that we cannot stay focused on the issue. And I think that every member who wanted to participate has had the opportunity in public hearings,

also in private meetings with DOE, to ask questions specifically about the decision to release SPR. Mine are more with the comments of Mr. Largent, and that is how do we fix it so we get it right.

Let me move to a comment that Mr. Summers said in his memorandum to the President. It was his last point where it talked about the benefits and the down side. His last point was engaging in a large SPR exchange would increase the sense of administration ownership of oil prices. It would set a dangerous precedent that would put pressure on all future Presidents and call into question our commitment to the free operation of this market. I think that is why a majority of the members are involved in this hearing. Whether it is a Republican or Democrat that occupies the White House, we want to make sure that the guidelines on the use of SPR are clear, that they can't be used to manipulate price or to get an advantage politically. That is not what it is there for. It is there to address whatever the criteria is that is set up in legislation.

And we can argue back and forth as to whether the right section of the statute was used by the Secretary to release the barrels, but in the absence of it being clear today, then there is a compelling reason for this committee to ask you questions, to hold this hearing and additional questions, and to make sure that no other administration is unclear about the use of SPR and how we go about that.

Let me ask you several questions. Why did the administration agree to release SPR barrels?

Mr. KRIPOWICZ. The basis we have been following since last winter, the heating oil supplies, particularly in the Northeast, and people have been urging us for other reasons, for gasoline supply shortages and for higher prices, to release oil from the Strategic Petroleum Reserve since last January.

Mr. BURR. To my understanding we have not had a gasoline shortage. I don't know of any areas that ran out of gasoline. We have had high prices.

Mr. KRIPOWICZ. And very short stocks, but there were no shortages, that is correct, low stocks.

Mr. BURR. So was the reason gasoline pricing or gasoline shortages?

Mr. KRIPOWICZ. I think the specter of shortages and the high prices were why people were asking the administration to take a look at releasing the Strategic Petroleum Reserve. But what we have been doing is following the heating oil process since last January. In July, because inventories were still low, we established a heating oil reserve in case there is an actual emergency shortage this coming winter, and that reserve is full. As the administration continued to watch the stocks of heating oil, we found that they continued not to grow. And as a matter of fact, they are still, the primary stocks are still decreasing at this point.

Mr. BURR. Do we have U.S. Oil companies that currently export heating oil?

Mr. KRIPOWICZ. Yes, there is some export of heating oil in the neighborhood of somewhere—

Mr. BURR. So at a time when we release 30 million barrels of the SPR to address a heating oil shortage in New England, U.S. companies are refining heating oil and exporting it around the world?

Mr. KRIPOWICZ. And we have heating oil imports also.

Mr. BURR. Which leads me to where Mr. Largent was with you, sir, as it relates to our inability to determine where oil goes. Though we might be able to track through export requests these 30 million barrels of refined product, we actually have no way of knowing what might have been diverted from a company's import into the United States to another area of the world where they decided to send them refined product or crude oil; is that correct?

Mr. MAJAK. I think that is correct. With our present level of data collection and monitoring, that is correct.

Mr. BURR. Let me ask you, who was openly opposed in the administration to the opening of SPR?

Mr. KRIPOWICZ. My recollection is that you have a memorandum from the Secretary of the Treasury that predated the release, but I am not aware of anybody once the release was made.

Mr. BURR. Were you aware of that memorandum to the President prior to me mentioning it?

Mr. KRIPOWICZ. It was brought up in the previous hearing.

Mr. BURR. Were you aware of the memorandum to the President by the Secretary of Treasury prior to any Congressional hearings?

Mr. KRIPOWICZ. I was personally not, but I cannot tell you who in the administration was aware of that.

Mr. BURR. What degree were you involved in the decision to release SPR?

Mr. KRIPOWICZ. My office was involved in that decision, but I was not personally involved in many of the aspects of it.

Mr. BURR. Were you in favor of it or were you against it?

Mr. BARTON. Or were you even asked your position?

Mr. KRIPOWICZ. From the Strategic Petroleum Reserve office, which is part of my organization, we have provided information that would indicate that the exchange of crude would get us increased supplies for this Strategic Petroleum Reserve and we would be in favor of doing that.

Mr. BARTON. I do not think that is a direct answer.

Mr. BURR. Yes or no, were you in favor of it or not?

Mr. KRIPOWICZ. Yes.

Mr. BARTON. And you were asked as Acting Assistant Secretary?

Mr. KRIPOWICZ. I was not involved in the final decision but I was aware—

Mr. BARTON. So you supported the decision, but you were not asked about it?

Mr. KRIPOWICZ. I wasn't asked specifically—

Mr. BARTON. And that is a straight answer. You are becoming political. Your learning curve is much too rapid.

Mr. BURR. I don't want to put you on the spot, but I would be remiss if I did not ask you this. But you were in favor of this before or after the decision was made?

Mr. KRIPOWICZ. Before.

Mr. BURR. Let me go back to the history of SPR releases and just ask you for your comments. In the 1991 release during the Persian Gulf War we required earnest money. We moved to the 1996-1997 sale, where no earnest money was required in the bid process. In September we required no earnest money. Now we have flipped

back in our October bid process to requiring earnest money up front.

Why did we go through a 9-year span where earnest money was not important and now return to a period where earnest money is important?

Mr. KRIPOWICZ. There are two reasons why. One is that because of the publicity that this part of the process has received to date, the original solicitation, we believe that because of the access to Internet and the wide publicity that has been gotten here that many inexperienced or unqualified bidders would probably apply in a second round if we did not put some sort of minimum bid requirements. So we fashioned a requirement that we believe will still allow legitimate small businesses, whether they have experience in the oil industry or not, to apply.

Mr. BURR. You also changed another very important part of that bid if my numbers are correct. In the September 2000 bid the irrevocable letter of credit was for 100 percent of the value of the contract. In the October 2000 bid you are now requiring that the irrevocable letter of credit be for 110 percent of the value. What precipitated that change?

Mr. KRIPOWICZ. It was our feeling that we wanted to protect whatever premium might be offered as well as the original amount of the Strategic Petroleum Reserve, which was the basis of the 100 percent letter of credit.

Mr. BURR. So in other words, a determination was made based upon who you saw bidding on the process, that if somebody defaulted, even though you had a letter of credit for 100 percent, you did not have the extra 3 or 4 or 5 percent under the swap; is that correct?

Mr. KRIPOWICZ. That is correct.

Mr. BURR. So was there a belief within the Department of Energy based upon the bidders that you saw that you were concerned whether individuals would default?

Mr. KRIPOWICZ. I think it was just out of an abundance of caution.

Mr. BURR. Why did that caution not exist under the structure of the September of 2000 bid? Because clearly the last sizable sale in fiscal year 1996 required 110 percent of the contract in the letter of credit.

Mr. KRIPOWICZ. Actually on an exchange we had never required the bid bonds until now.

Mr. BURR. Bid bonds and the letter of credit are two different things.

Mr. KRIPOWICZ. Right.

Mr. BURR. The bid bond is up front prior to the bid being submitted. The letter of credit is the guarantee. As it related to the September 2000 process, you gave them a period of time after the bid was accepted to produce a letter of credit.

Mr. KRIPOWICZ. That is correct.

Mr. BURR. That letter of credit was for 100 percent of the value of the SPR that was released to them. Now that letter of credit must be for 110 percent of the value of what they got. That is a substantial difference.

Mr. KRIPOWICZ. Yes, it is.

Mr. BURR. What motivated that change?

Mr. KRIPOWICZ. To err on the side of caution with regard to the value of the ability to replace the premium oil—

Mr. BURR. So of the 23 million barrels that we released under the original contract, if they were to default we would only get the value of the barrels that they took; we would not get the profit of what they bid, which was the increased barrels that comes out of the swap?

Mr. KRIPOWICZ. That depends on price. We might and we might not. And that is the reason for putting the 110 percent requirement on that.

Mr. BURR. I think that is one of the reasons that the Chairman of the Federal Reserve and the Secretary of the Treasury wrote their letter, was that they were concerned with the Federal Government and the role that the release of SPR might have in artificially affecting the marketplace on petroleum. Not short term, which was what you expressed that you were after, and that was some price relief. Their concern was long term and the President of the United States government influencing the futures of petroleum or any other commodity in the marketplace.

Mr. BARTON. The gentleman's time has expired.

Mr. BURR. Since we are the only ones here, could I take 1 additional minute and you and I run for the vote?

Mr. BARTON. I will stay until Mr. Pickering comes back.

Mr. BURR. Then I would be happy to stay here with you if I can have an additional minute.

Mr. BARTON. You may have an additional minute, but I have a few questions, too.

Mr. BURR. Mr. Secretary, the letter from Secretary Summers said that the proposed sale of 60 million barrels—was originally the proposed release from SPR 60 million and not 30 million?

Mr. KRIPOWICZ. There was discussion of other quantities, yes.

Mr. BURR. Were you in favor of 60 million?

Mr. KRIPOWICZ. I was in favor of a substantial release of oil, and it was determined to release 30 million barrels and to wait and see what the effect was.

Mr. BURR. Was there a request by the administration for a release of 60 million barrels?

Mr. KRIPOWICZ. I don't know the exact answer to that.

Mr. BURR. Did Mr. Summers just come up with 60 million at random?

Mr. KRIPOWICZ. My assumption is that those quantities were discussed within the administration.

Mr. BURR. Was your office involved in the decision as it related to the amount of barrels that were released from SPR?

Mr. KRIPOWICZ. We provided information that—what we could do with regard to what kind of oil we could get on to the market and those—

Mr. BARTON. Would the gentleman yield?

Mr. BURR. I would be happy to.

Mr. BARTON. We have documents that have been provided by the policy office that indicate there was a substantial discussion for releasing a million barrels a day for 60 days, and there were computer models run about the price impact, and there was significant

discussion about the price impact on the market and very little discussion about the amount of fuel oil that would be ultimately made available.

Mr. BURR. In fact, the Secretary of the Treasury made in his memorandum to the President that under 60 million barrels released from SPR, as it related to fuel oil, he projected it would have a 2.6-cent per barrel—per gallon drop. Now that we have released 30 million barrels, which is half, I would assume we could extrapolate that the savings would be half of the 2.6. So is the attempt by the Department of Energy through the SPR release to bring 1.3 cent per gallon relief to those users of fuel oil?

Mr. KRIPOWICZ. It was an attempt to get more oil into the market.

Mr. BURR. Is Secretary Summers' projections on the savings to the system of 1.3 cents per gallon, is that an accurate number?

Mr. KRIPOWICZ. I don't know whether that is accurate or not. Those are not my calculations.

Mr. BURR. What would your calculations be?

Mr. KRIPOWICZ. I didn't do those calculations.

Mr. BURR. Did the calculations of price savings play any part in your particular department's decision as to whether you were for or against SPR release?

Mr. KRIPOWICZ. There is obviously some effect on price but that was not the main thing that was looked at. It was whether we could actually get, as we have discussed here, heating oil into the market and that is what the analysis—

Mr. BURR. Clearly as it relates to the Secretary's usage of the release of SPR, he couldn't do it for the price reasons and use the argument he has from the standpoint of why it was released. And I would remind all of my colleagues that we have never declared an emergency, and that is why we have used a swap. I thank you for your patience. I thank the chairman for his.

Mr. BARTON. I intend to keep the hearing going. Mr. Pickering is supposed to come back. So I will ask some questions until he gets back, and then he will ask questions. Then we will go to the next panel because I know that Admiral Watkins has an airplane that he needs to take.

I want to ask both of you gentlemen about the Jones Act. I have introduced legislation that Congressman Boucher has cosponsored to provide a 90-day waiver upon date of enactment to give the President the discretion to allow the transport of fuel oil from one port to another port in the United States if he feels it is necessary to get supplies into the Northeast, although it says port to port. It is a 90-day waiver. It is temporary. What would the administration's position be on that act? Either one of you gentlemen.

Mr. KRIPOWICZ. We would have to get back to you on what the administration's official position is, but at this point we know of no request for Jones Act waivers, and if we get them the Department of Energy has worked very hard to try to expedite those. If this would expedite the procedures, I would expect, all other things being equal, it would be a good thing.

Mr. BARTON. The committee staff has been told and there have been press reports that there is a non-availability of U.S. Flag carriers to move the oil. So this would be another discretionary tool

to give the President the ability to allow for a waiver if that would in fact help to expedite deliveries. Does the Commerce Department have any reaction?

Mr. MAJAK. Mr. Chairman, I have not personally been involved in any of those discussions, so I really can't shed much light on this question.

Mr. BARTON. We just put the bill in yesterday. We haven't publicized it, but it is something I would like to have you all check with your appropriate officials and get back to us because if we are going to do this, we will have to put it on the suspension calendar next week, and eventually I hope Congress adjourns for this year.

I do want to ask the question of Mr. Kripowicz more than Mr. Majak. On this Northeast fuel oil reserve we have 2 million barrels in it, I think, or 2.2 million barrels. The legislation in the House to authorize it gives the President quite a bit of flexibility on using it on a regional basis, does not require a national emergency, quite a bit of discretionary authority.

Why wouldn't the President right now want to authorize the release of some of the fuel oil reserve, if you are really concerned about fuel oil in the Northeast? You have 2 million barrels in the reserve that is put there explicitly for supply problems in the Northeast. Why not, instead of going through this, you know, indirect route, why not be direct?

Mr. KRIPOWICZ. Because at this point, even with the authorities that are in the proposed EPCA, there is no actual supply interruption right now, nor are there the price spikes that are included in the trigger mechanism.

Mr. BARTON. Well, if that is the case, then it begs the question, why go through what you have already gone through in releasing the SPR, if, in fact, you released the SPR to get more home heating oil, then you have a direct resource that is right there. If, on the other hand, you didn't release the SPR for home heating oil, you used it to influence the market for price, then that is a wholly different issue, and releasing home heating oil from the reserve has no impact on world oil markets. Would you agree with that?

Mr. KRIPOWICZ. I would guess that because it is 2 million barrels of heating oil, it would have little impact on world—

Mr. BARTON. But you agree that 2 million barrels is a bigger number than 250,000 barrels.

Mr. KRIPOWICZ. I do, but it is held for emergency purposes. The thing about the heating oil reserve, or the release of the SPR oil is that it is meant to build heating oil inventory so that we don't have to get into emergency situations where we would have to release the Reserve.

Mr. BARTON. Well, there has been no testimony—

Mr. KRIPOWICZ. The government gets its oil back, and then some.

Mr. BARTON. There has been no testimony at this hearing or the hearing 3 weeks ago that have indicated we have any major emergency situation, even in the Northeast, for home heating oil. There has been testimony that indicates that the supply levels, the stocks, the inventory levels are below where they normally would be.

Mr. KRIPOWICZ. Yes, sir.

Mr. BARTON. And there were some questions about maybe this is just the market changing and they are going to maintain lower heating stocks. Maybe that is just a natural result of higher prices that extend into the future. Everything that has been put out publicly talks about the impact in lowering prices, but since that is not allowed by law, all the official testimony is, oh, we are doing this as a swap for in the future, to get more oil in, although there has been no debate about that last summer, there has been no message to the Congress about that, about we want to put more oil in the Strategic Petroleum Reserve.

So I am very skeptical, if you have a home heating oil reserve that could be used this winter in which the President sends a message to the Congress saying I would like to use it, I think it passed in the House and in the Senate without opposition. I would support that. Nobody wants home heating oil to be not in supply or to be at a supply that is so high that people can't afford to pay it. That is why we have not objected to the LIHEAP program. There has been no policy objection to any of the real efforts to help low-income folks in the Northeast with home heating oil, or natural gas for that matter.

You could use LIHEAP to pay for natural gas as well as home heating oil. But there has been a lot of objection from myself and others about politicizing the SPR a month and a half out before the election and using it for a purpose which it was not intended, which is to affect the price in the world market. It was never intended for that. Do you agree with that?

Mr. KRIPOWICZ. It wasn't released to affect the price.

Mr. BARTON. Well, now, we have all kinds of documents that were put in the record that talk about that.

Mr. KRIPOWICZ. It is not the primary effect. Everybody knows that it would have some effect on the market, at least on a short term basis, but the fact that heating oil reserve stocks in the Northeast are 70 percent below last year's levels, something was said that in addition to the heating oil reserve, we needed to do something else to get heating oil into the Northeast and into stocks in the Northeast, and this was the only other choice that the President had.

Mr. BARTON. Well, I will say again, that the minority is not here, so we will not put this document into the record until they have reviewed it and allowed it to be put into the record. But on August 24 there is a memorandum to Secretary Richardson from Melanie Kenderdine, who is the Director of the Office of Energy Policy at the Department of Energy. On page 2, it talks about an exchange of 1 million barrels per day for 2 months would decrease per dollar oil prices by 1.70 and by March of next year would decrease the price per barrel to around \$24.

Now, what little documentation that has been presented by the Department of Energy, there is all kind of this type of information where before the decision was being made, you are talking about the price volatility of the market and how it impacts the market in terms of prices, and there is some discussion about home heating oil, but that discussion basically, as I have pointed out earlier, says, it is really not going to do much. It is an indirect way to get home heating oil. But again, that is the political cover to allow you

to go in and—not you personally, but to allow the administration to go in and manipulate the market. How can you sit there with a straight face and not admit that? You are an honest man.

Mr. KRIPOWICZ. And I honestly know that we will get more heating oil out of this for the Northeast.

Mr. BARTON. You are going to get 250,000 barrels, using your numbers, additional home heating oil. That is about—

Mr. KRIPOWICZ. For oil that can only be used in the heating oil market.

Mr. BARTON. One barrel a person. I don't know how many homeowners use home heating oil, but it is probably more than 250,000 of them, so they will get one additional barrel of home heating oil or maybe a half a barrel, who knows.

Mr. KRIPOWICZ. I will submit that they will also get a significant portion of that 70 percent of the barrels that go for highway diesel also; if there is a demand for the oil, that they will get it.

Mr. BARTON. Well, if they do, then your diesel owners are going to be petitioning the Department of Energy and the President that these prices are going to go up and you are going to be right back in the same box. You know that and I know that.

Mr. KRIPOWICZ. But this is additional supply, this isn't supply that was already expected to be on the market.

Mr. BARTON. I am going to yield to the gentleman from Mississippi and after his questions release this panel and start the second panel.

Mr. PICKERING. Thank you, Mr. Chairman. Mr. Kripowicz, let me just walk through a series of questions. As you were talking to the gentleman from Virginia, Mr. Boucher, you talked about, as you accepted the bids that you all did, your due diligence of investigation of the bidders, of looking at their financial capability, their business background, and their potential partners; is that correct?

Mr. KRIPOWICZ. Yes, that is correct.

Mr. PICKERING. What was your sequence of doing such an investigation? Before you accepted the bids, did you do your due diligence?

Mr. KRIPOWICZ. Yes, we did.

Mr. PICKERING. And so your answer today is that the gentlemen that have been highlighted in various articles, you did a due diligence background investigation on them before you accepted their bids? Is that your testimony?

Mr. KRIPOWICZ. We did do due diligence and we got whatever information we possibly could, including evidence that they were in serious negotiations with people in the oil industry.

Mr. PICKERING. Was that before you accepted their bids?

Mr. KRIPOWICZ. Yes.

Mr. PICKERING. Before? That is your testimony, before you accepted their bids?

Mr. KRIPOWICZ. Yes, it is.

Mr. PICKERING. Now, it seems to me logically, if you are going to have a well-run program, that maybe you would accept bids, you would have this line of credit criteria, and if they couldn't meet that criteria, then you would do something differently like you did, you eventually went other places for those millions of barrels where you accepted these other bids. But it is hard for me to comprehend

a program where you would take the three, with their backgrounds, with their financial capabilities, with their financial resources and accept their bids, that you did due diligence before you accepted their bids.

Mr. KRIPOWICZ. Well, one of those three has a contract, and novated the contract to another company in the oil industry and we are delivering the 3 million barrels. The other two, we were in serious negotiations right up to the last minute, because we were in contact with the people that they were dealing with on an almost daily basis.

Mr. PICKERING. Based on the articles again that have appeared in the print media, those negotiations only began after they were awarded the bids; is that not correct?

Mr. KRIPOWICZ. The serious negotiations—

Mr. PICKERING. Before, before, before you accepted their bids?

Mr. KRIPOWICZ. That is my understanding, yes.

Mr. PICKERING. That is your testimony?

Mr. KRIPOWICZ. That is my testimony.

Mr. PICKERING. You are sticking to it?

Mr. KRIPOWICZ. Yes, I am.

Mr. PICKERING. They were in negotiations before they did.

Mr. KRIPOWICZ. Yes.

Mr. PICKERING. So if we contacted those three and asked them when negotiations started, they would testify as you do, consistently with what you testify, that they were in negotiations before they bid?

Mr. KRIPOWICZ. I don't know whether they were in negotiations before they bid—

Mr. PICKERING. You just testified to me that they were in negotiations prior to their bid, that you did due diligence, and you—

Mr. KRIPOWICZ. Prior to our acceptance of their bids. I didn't say before they bid. I have no knowledge of what they did before they bid.

Mr. PICKERING. Okay. But you did due diligence, they provided you with—and you received information that you can verify that serious negotiations were ongoing as you accepted their bids?

Mr. KRIPOWICZ. Yes. We had indications and evidence of serious interest from people in the oil industry, that is correct.

Mr. PICKERING. It appears to this committee, though, and it appears to the public that this was a politicized decision, that it was a politicized decision in the heat of a campaign on the spur of the moment, after previous decision points had been reached where this option had been rejected; but as the campaign heated up, the Vice President makes a decision to recommend, or come out in support at least of SPR, and the next day the President adopts his position, and then you were tasked with implementing that political decision and to do it in such a way that really doesn't make much sense. It doesn't seem to be well-executed or well-implemented, and raises the examples that we have been talking about today where it really doesn't make sense from the common public, to other media who have covered this, that this is the way the government should run.

So I understand why we are concerned today and why I am asking, did you do your due diligence before or after receiving these bids?

Let me go in another line of thought as well. You testified earlier that we now have 57 days of supply in our Strategic Petroleum Reserve; is that correct?

Mr. KRIPOWICZ. Yes.

Mr. PICKERING. Combined with private stock, you say over 120 days of supply?

Mr. KRIPOWICZ. Approximately, yes.

Mr. PICKERING. Now, our European and Japanese allies have the right to go into those private stocks and use them in cases of national emergency, or national security; is that correct?

Mr. KRIPOWICZ. What was the question again?

Mr. PICKERING. The other members of the IEA are different than we are. They have either government stocks similar to our Strategic Petroleum Reserve, or they have the right to call or to draw down from private stocks; is that not correct?

Mr. KRIPOWICZ. I don't know the answer to that question.

Mr. PICKERING. You are the Assistant—just a second. Let me make sure I understand here. You are the Assistant Secretary of Fossil Fuel, is that correct?

Mr. KRIPOWICZ. That is correct.

Mr. PICKERING. And you do not know what the policies are of our international partners where we coordinate with IEA, when we face possible strategic shortages, our national security disruption of our oil and energy supplies, you do not know what the policies of our foreign policies are, our international partners are?

Mr. KRIPOWICZ. Some of our international partners don't even have strategic stocks.

Mr. PICKERING. Yes, but they do have the right to call private stock, is that not correct?

Mr. KRIPOWICZ. The ones that do have government stocks that are held in private storage. That is my understanding.

Mr. PICKERING. So they combine both private and public?

Mr. KRIPOWICZ. We choose not to do that.

Mr. PICKERING. That is correct. Which means, obviously, that the logic and the intent of the Strategic Petroleum Reserve authorization was that we were a government stock only.

Mr. KRIPOWICZ. No, sir.

Mr. PICKERING. Because we do not have the right to call the stocks from private supply, is that correct, in this country?

Mr. KRIPOWICZ. We do. EPCA has the authority to have industrially held stocks.

Mr. PICKERING. Have we ever used that authority?

Mr. KRIPOWICZ. We have not.

Mr. PICKERING. What was—the authorization and the original intent of the Strategic Petroleum Reserve was to have a government-only, 90-day supply, not a combination of private and public stock?

Mr. KRIPOWICZ. That was the goal, from my understanding.

Mr. PICKERING. And that was the intent. But you have used a fairly broad and liberal interpretation of combining private and public when we have no authority, no ability to call private stock.

Mr. KRIPOWICZ. The Strategic Petroleum Reserve is only—

Mr. PICKERING. Has never been used.

Mr. KRIPOWICZ. The Strategic Petroleum Reserve is only authorized for 1 billion barrels if our demand goes up, and that will be less than 90 days worth of protection anyway.

Mr. PICKERING. A last series of questions.

You had testified, as I believe Mr. Barton and Mr. Burr asked you about, what your personal position was, of whether this was a good policy decision or just a political response. I worked in the Bush Administration for 2 years and I understand that usually the technical office and the staff that manages and administers particular programs are asked as decisions are pending what their recommendations are, what the outcomes or options of each option would be, and they then send that to the Secretary, to the White House, and they coordinate with an interagency process; for example, the Treasury Department.

Did you produce any memos to the Secretary during this decision process or prior to the decision that was made that came through the Strategic Petroleum Reserve office and through you as the Assistant Secretary, did you produce any memos to Secretary Richardson?

Mr. KRIPOWICZ. I don't know the direct answer to that question. There was documentation that was provided from our Strategic Petroleum Reserve office to the committee, and we are researching our records to find out whether any additional information is available. If it is, the committee will receive it.

[The information had not been received at time of printing.]

Mr. PICKERING. Will this be the same old story, the same old dance, the same old tune of we are trying to find our files, we just misplaced them somewhere?

Mr. KRIPOWICZ. The Department has provided—over the years, the Department has provided reams and reams of information to the committee and I don't believe has ever said that we haven't been able to find any.

Mr. PICKERING. It seems to me that when a decision of this importance is made, that there would be—the memos would be readily accessible and available, any memo or correspondence that went to Secretary Richardson, I am sure, would be something that the Strategic Petroleum Reserve office would have on file and readily accessible.

Mr. KRIPOWICZ. And we have provided the memos more normally to the policy office, and those memoranda and e-mails have been provided to the committee, the ones that we have at this point.

Mr. PICKERING. And on any of those memos, did you all make a recommendation for or against release from the Strategic Petroleum Reserve?

Mr. KRIPOWICZ. My recollection, and it is only my recollection, because I don't have the documentation in front of me, is that we were the—the responses that we were providing were technical questions on our capabilities.

Mr. PICKERING. But no recommendations?

Mr. KRIPOWICZ. We were not—we did not submit any recommendations in writing, that is correct.

Mr. PICKERING. In favor or in opposition?

Mr. Burr, do you have any additional questions? I yield back to you, but I would like to follow up briefly.

Mr. BURR [presiding]. You can go ahead with additional questions now, or I will take the opportunity now and come back to you.

Mr. PICKERING. Just one final question.

Since the release of the SPR, the price of home heating oil has gone back up. It came down for a period of time and now is going back up, is that correct?

Mr. KRIPOWICZ. Yes, that is correct.

Mr. PICKERING. So basically we have a political decision, poorly executed, poorly implemented, poorly administrated, and the objective effect of this was either substitution or other outside events. Was there any coordination—let me ask this question. Was there any coordination with our Japanese and European allies for them to release from their stocks to address this international crisis?

Mr. KRIPOWICZ. This was not an emergency release, so that coordination wasn't necessary.

Mr. PICKERING. I thought your authority was only for an emergency release.

Mr. KRIPOWICZ. This is an exchange, this is not a sale, so the President did not have to declare an emergency.

Mr. PICKERING. Why is—if this is so important for us domestically then, even if it is not an emergency, why would you not coordinate with your European and Japanese allies?

Mr. KRIPOWICZ. There were discussions with international, and particularly European countries that I am not party to, but I know there were discussions with them.

Mr. PICKERING. And the outcome of those discussions were?

Mr. KRIPOWICZ. I don't know the answer to that, except there were press reports that some European countries were also considering releases.

Mr. PICKERING. But they have not done that?

Mr. KRIPOWICZ. They have not done that.

Mr. PICKERING. So we were not effective or persuasive with our allies to follow this wise policy that the U.S. took, is that correct?

Mr. KRIPOWICZ. That was not the intent of our discussions with them.

Mr. PICKERING. So it was not your intent, if this is an important issue, domestic issue and international issue, for the health of our economy and our consumers in the Northeast, if it is this important—or is it just for political campaign purposes, not really that important? Is that why we don't do something with our international allies, if it is not a real effect, economically or otherwise, or strategically? Is that why we didn't coordinate better with our allies?

Mr. KRIPOWICZ. The reason for the release was to build heating oil stocks in our country, not to build heating oil stocks anywhere else, and we had discussions with our allies and made the decision to go ahead with our release, our swap of oil in order to try to build heating oil stocks in the Northeast.

Mr. PICKERING. Isn't this an unprecedented use then of our Strategic Petroleum Reserve and what it was intended to do, and now it has become the home heating oil reserve of the Northeast? Isn't this unprecedented?

Mr. KRIPOWICZ. No, it isn't unprecedented. We have had exchanges before to take care of supply problems or potential supply problems.

Mr. PICKERING. And that was in the Persian Gulf, is that correct?

Mr. KRIPOWICZ. No. This was on the Gulf Coast, in particular. Three different times we exchanged oil.

Mr. PICKERING. For what purpose?

Mr. KRIPOWICZ. Because—

Mr. PICKERING. That was more of an operational—

Mr. KRIPOWICZ. There were potential supply shortages for two refineries, in one case when we were producing into a tight gasoline market this summer, and there was a potential oil pipeline shutdown that was averted by providing oil in exchange several years ago, and we also have exchanged oil when receiving oil, royalty in kind, from the Gulf Coast last year.

Mr. PICKERING. And what was the scope? How many—on those swaps, how many barrels would you do?

Mr. BARTON. The gentleman will have to make this his last question.

Mr. PICKERING. I am just wanting to understand the precedent we are setting here.

Mr. KRIPOWICZ. Overall, it is about the same magnitude of this particular swap. The royalty in kind exchanges were in the neighborhood of 28 million barrels. The other ones were in the neighborhood of 1 million barrels each.

Mr. PICKERING. Was that part of the decommissioning of the Weeks Island site?

Mr. KRIPOWICZ. No.

Mr. PICKERING. No, that was different.

Mr. Burr, thank you.

Mr. BURR. Mr. Secretary, let me ask you one last question and then we do need to move on to the next panel.

What was the reasoning at the Department of Energy for using section 6240(a) for the release of the oil?

Mr. KRIPOWICZ. Is that section 160?

Mr. BURR. Yes, I think it is 160.

Mr. KRIPOWICZ. 160(a), because that gives the Secretary the authority to acquire oil by exchange.

Mr. BURR. And if you had chosen another section, would that not have triggered some findings by the President or a report to Congress by the Secretary?

Mr. KRIPOWICZ. Yes, that is correct. If we were to have declared an emergency, it would have required the findings to be presented to the President for him to make.

Mr. BURR. Was there an internal discussion within your Department or within the Department of Energy relative to why they chose to exercise a swap versus to declare the emergency and to make a report to Congress?

Mr. KRIPOWICZ. At this point, we felt that it was not an emergency situation, we couldn't point to an actual shortage. There have been various looks over the past year because of the fluctuations in the supply in the market as to whether any of those conditions meet emergency requirements, and the assumption has been to this point that they do not.

Mr. BURR. The Chair would only make this comment and then let you go. Many times your answers today have suggested a significant sense of urgency in the need for us to do this. Certainly the paper trail that follows this year-long attempt by this committee to understand what the administration's intent and the Department of Energy's intent as it related to SPR sales in a period where we have gone through that we have known were shortages as we came off of last year, shortages that we predicted for this year, price spikes that were predictable, yet some suggest that it was not. We have tried to monitor the process along with the Department of Energy. We have asked questions along the way.

Something changed. Something changed in a very short period of time. In your answers, if you haven't used emergency, you have used words that could interchange with it, but certainly there was a new increased sense of urgency. You have been very eloquent in the fact that you said this was not for price stability, because we know that would trigger some other things. But the reality is that this is about as close to a declaration of emergency, and I think every Member of this committee has a right to question whether the choice of the section that was used was because the administration did not want to send a report on findings and the Secretary did not want to send a report to Congress. That is something that will remain unknown.

The reality is that we are—this Member is glad to see that you have adopted in this new bid process a structure that we suggested privately to the Department of Energy before they had received bids, before after they had set up a structure as it deals with the amount required in guarantee, and the requirement that people be preapproved. And I think your statement earlier, though I am not an expert as it relates to the bonding process; I actually wouldn't think that there is a cost involved in that letter of credit until the letter of credit is exercised. If, in fact, there is, it is because there is not a relationship with that individual and lending institutions. So the requirement to have preapproval or some bonding that allows them to bid that says they do have access to the letter of credit I don't think is a financial disadvantage to any person, whether it is a company or an individual in the marketplace to have bid on this product.

Once again, I want to thank you on behalf of all members of this committee, to both of you, for your testimony today. At this time we release the second panel.

Mr. MAJAK. Thank you, Mr. Chairman.

Mr. BURR. At this time I would like to call up the third panel and final panel.

This panel is made up of Admiral James Watkins, U.S. Navy Retired, President of C.O.R.E.; Mr. Neil Wolkoff, Executive Vice President, New York Mercantile Exchange; John Manzoni, President, Eastern United States BP; William Martin, Chairman of Washington Policy and Analysis; John Surma, Senior VP, Supply and Transportation, Marathon Ashland Petroleum; and Mr. John Boles, President of Equiva Trading, part of Equiva Services.

Let me welcome our entire panel and ask everybody just to take a seat as soon as its possible.

The Chair at this time welcomes Admiral Watkins. We realize that you do have a time constraint. We apologize for the length of the first panel.

If there is no objection, the Chair would like to recognize Admiral Watkins for 5 minutes for his opening statement and allow any members who wish to question him to do so, and then we would return to the regular order of opening statements of the rest of our witnesses.

Admiral Watkins.

STATEMENTS OF JAMES D. WATKINS, PRESIDENT, C.O.R.E.; WILLIAM F. MARTIN, CHAIRMAN, WASHINGTON POLICY AND ANALYSIS; NEIL L. WOLKOFF, EXECUTIVE VICE PRESIDENT, NEW YORK MERCANTILE EXCHANGE; JOHN P. SURMA, SENIOR VICE PRESIDENT, SUPPLY & TRANSPORTATION, MARATHON ASHLAND PETROLEUM, LLC; JOHN MANZONI, PRESIDENT, EASTERN UNITED STATES BP; AND JOHN BOLES, PRESIDENT OF EQUIVA TRADING, EQUIVA SERVICES

Mr. WATKINS. Thank you very much, Mr. Chairman, members of the subcommittee. In your invitation for me to testify before you today, you requested that I address a number of concerns that have recently emerged in regard to the administration's oil policy and its decision to tap the Strategic Petroleum Reserve. I will refer to that as the SPR. I believe, as does Treasury Secretary Summers, that the administration's SPR decision was ill-advised as a matter of policy, poorly implemented, and likely futile as a means of mitigating prices in the heating oil market.

The SPR is not a tactical weapon, but a strategic one, designed and built with a clear intent of responding to major supply disruptions that, in the intent of the enabling legislation, would likely cause irreparable harm to the Nation and its economy. It was properly used during the Iraqi war, precisely for the purpose of responding to a supply disruption of over 3.5 million barrels of oil a day, while the threat existed to more than half of the additional Saudi production capacity. That particular decision, consistent with the intent of SPR's enabling legislation, was taken in the wake of extensive consultation with allies and subsequent to the completion of other critical steps designed to maximize the effect of the SPR release, once it came.

It is useful to reference the decisionmaking process that led to the 1991 SPR use because it illustrates the differences with the present administration's approach to oil policy. We managed the Iraqi crisis by first focusing on conservation and demand reduction and launching a national campaign to reduce consumption by about one-half million barrels a day.

Second, we met with each of the U.S. oil producers and their trade associations to request a surge in production from all available domestic supplies.

Third, we met with allies among Persian Gulf producers to fully account for their production capacity and plans, and to establish private communication channels allowing for instantaneous exchange of vital production information.

Fourth, we secured a blanket waiver of Jones Act requirements in order to ensure that transportation bottlenecks would not ham-

per the seamless flow of oil, especially from the U.S. Gulf Coast to the vulnerable northeast.

Finally, we ran live and desktop tests of the SPR response mechanisms, including prequalification of all potential bidders, in order to eliminate glitches in the system before the actual drawdown.

Mr. Chairman, the SPR drawdown of 1991 stands in obvious contrast to the administration's decision of 2 weeks ago to use the SPR as a knee-jerk response to market fundamentals that have been created by the administration's own 8 years of oil sector benign neglect. We, as a Nation, are worse off than we were in 1991 because demand for oil is substantially higher, as is reliance on insecure supplies of oil. There would appear to be no apparent diplomatic strategy to address newly aggressive OPEC behavior. Administration policy has made no difference to domestic oil production, or to domestic oil consumption; neither to fuel switching in the vulnerable New England, nor to enhanced refining capacity nationwide. We have, in sum, squandered the 4 years of strong, bilateral policy conduct that led to the enactment of the Energy Policy Act of 1992 and can now respond to oil sector issues only with Band-Aids and palliatives.

Mr. Chairman, only a few months ago, you asked me to testify before this subcommittee as to the adequacy of the Nation's energy policy. I gave you my views on 24 May as to why I felt that we had allowed all of our good bipartisan work of the early 1990's to lapse. We do not have what can reasonably be called a meaningful energy policy in this country. I will not repeat the specifics of my position, because they are a matter of Congressional Record. I will say that I have detected no sense of purpose or urgency in the crafting of national energy policy for the last 8 years. The administration's benign neglect of the oil sector remained undisturbed until the crude prices increased in this very critical political year.

The fact of the matter is that the northeast fuel market cannot be changed either by the chronic releases of the SPR, nor by the creation of the fuel oil reserve that has been established by the administration. To change the northeast's exceptional over-reliance on fuel oil for heating, action will be needed at a structural level and through determined Federal and State policy to change the fundamentals of that dependence.

For the immediate term, the more effective means of getting more supplies to the northeast for the winter, if that is really necessary, is another blanket Jones Act waiver, so that the ample supplies now in the U.S. Gulf Coast can be moved economically to the northeast.

For the longer term, the region's political leaders should look for solutions that do not shift the cost of their problems to the U.S. taxpayer. These include the construction of a state-of-the-art refinery in New England, expansion of the natural gas distribution system to accommodate more gas imports from the newly developed field of maritime Canada, and to provide economic incentives to encourage dual fuel capacity.

I will have to say, in listening to Mr. Markey this morning, I was extremely disturbed at the arrogance again of the northeast, which has been there now for 20 years on any new refining capacity going into that region. They don't mind using the refining outputs from

other States of our country; they don't mind them facing the environmental burdens, but not the northeast, how dare you put it in this pristine area of our country. Somebody ought to get the Governors together, get the Canadian representatives together, get DOE in the middle of it, get the futures market and the commodity market people together and sit down and solve this problem and start converting the northeast to natural gas. Over time it can be done. Let the existing reserve that is up there solve the problem in the interim, but get on with it like we have in the rest of the country.

We are not a Nation devoid of energy policy choices, but we do tend to avoid hard decisions on matters of crude oil supply and demand. The national energy strategy that I had the privilege of issuing in 1990 forecasts, as closely as it is feasible to do, the supply and demand equation that we have reached today.

I warned then and I warn now that without effective policy measures to reverse the trend we are on, we will revisit the issue of high and volatile energy prices henceforth and forever more. We can't change the fundamentals of the oil market by the expediency of the SPR or by building regional product stockpiles any more than we can change the fundamentals of the gas market by getting into the business of a Federal gas storage, nor can we do so by building Federal power plants to mitigate some seasonally high prices of electricity. On the other hand, we will change the fundamentals of the energy market by fostering increases in domestic production, deploying technology that reduces demand for fossil fuels, and by getting the Federal Government out of the price-fixing business.

Let me state unequivocally how inappropriate I believe the role of government is in what is generally considered a highly competitive oil market. That is that the SPR, which not incidentally was built and filled entirely during the Reagan and Bush Administrations, was created "to diminish vulnerability of the United States to the effects of a severe energy supply interruption." The Act also provides authority under which the United States may carry out its obligations under the International Energy Program. All of us in this room, and previous and current members of this committee, have repeatedly debated the criteria for use of the reserve, even as we have agreed on avoiding its use principally for the purpose of affecting prices in the marketplace, as was done in this case.

I am persuaded that the administration's release of SPR oil in this instance was used, as feared by Treasury Secretary Summers in his September 13 memorandum to the President, principally for the purpose of affecting prices in the marketplace. I consider not credible the administration's recourse to the fig leaf of low fuel oil inventories as rationale for the action.

In any case, even if worries about low fuel oil inventories were true, there is little the administration could do to precisely direct SPR oil toward fuel oil production. Indeed, the award of SPR oil contracts to traders devoid of experience in handling physical supplies of oil has severed whatever link there might have been between SPR oil availability and fuel oil production for the coming winter. As a matter of fact, the administration's election year intervention in the oil market is likely to produce no benefits at all be-

yond a transitory, entirely superficial shadow on prices. But it will set a terrible precedent for future SPR policy.

Mr. Chairman, the energy sector is unforgiving because it adheres to fundamentals of supply and demand and price and is immune to political expediency. Only in rare times since the first energy crisis of 1973 has this Nation taken the hard decisions that are the emblem of good policy. The last such time was in 1992 when very strong bipartisan leadership produced the Energy Policy Act. Even then, some decisions proved too difficult to make, even as the consequences of inaction intensified.

We have, Mr. Chairman, a second, untapped and unused SPR in the form of oil that lies buried within the Arctic National Wildlife Refuge. That oil can be produced with minimal impact on very small acreage. An increase in U.S. oil supplies is, in my view, essential to the achievement of a new equilibrium in U.S. energy policy, but not solely. We need robust diplomacy to deal with OPEC. We need effective investments in new technology. Most of all, we need leadership to avoid exposing ourselves repetitively to circumstances exemplified by this needless biannual regional dilemma.

Thank you, Mr. Chairman.

[The prepared statement of James D. Watkins follows:]

PREPARED STATEMENT OF JAMES D. WATKINS, FORMER SECRETARY OF ENERGY

Mr. Chairman and members of the subcommittee, in your invitation for me to testify before you today, you requested that I address a number of concerns that have recently emerged in regard to the Administration's oil policy, and its decision to tap the Strategic Petroleum Reserve (SPR). I believe, as does Secretary Summers, that the Administration's SPR decision was ill advised as a matter of policy, poorly implemented and likely futile as a means of mitigating prices in the heating oil market.

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It is useful to reference the decision-making process that led to the 1991 SPR use because it illustrates the differences with the present Administration's approach to oil policy. We managed the Iraqi crisis by first focusing on conservation and demand reduction, and launching a national campaign to reduce consumption by about one half million barrels per day. Secondly, we met with each of the U.S. oil producers and their trade associations to request a surge in production from all available domestic supplies. Thirdly, we met with allies among Persian Gulf producers to fully account for their production capacity and plans, and to establish private communication channels allowing for instantaneous exchange of vital production information. Fourth, we secured a blanket waiver of Jones Act requirements, in order to ensure that transportation bottlenecks would not hamper the seamless flow of oil, especially from the U.S. Gulf Coast to the vulnerable Northeast. Finally, we ran live and desktop tests of the SPR response mechanisms, including pre-qualification of all potential bidders, in order to eliminate glitches in the system before the actual draw-down.

Mr. Chairman, the SPR draw-down of 1991 stands in obvious contrast to the Administration's decision of two weeks ago to use the SPR as a response to market fundamentals that have been created by the Administration's eight years of oil sector benign neglect. We, as a Nation, are worse off than we were in 1991 because demand for oil is substantially higher, as is reliance on insecure supplies of oil. There would appear to be no apparent diplomatic strategy to address newly-aggres-

sive OPEC behavior. Administration policy has made no difference to domestic oil production, or to domestic oil consumption; neither to fuel switching in the vulnerable New England, nor to enhanced refining capacity nationwide. We have, in sum, squandered the four years of strong, bilateral policy conduct that led to enactment of the Energy Policy Act of 1992, and can now respond to oil sector issues only with band aids and palliatives.

Mr. Chairman, only a few months ago, you asked me to testify before this Subcommittee as to the adequacy of our Nation's energy policy. I gave you my views on 24 May 2000 as to why I felt that we had allowed all of our good bipartisan work of the early '90s to lapse. We do not have what can reasonably be called a meaningful energy policy. I will not repeat the specifics of my position because they are a matter of Congressional record. I will say that I have detected no sense of purpose or urgency in the crafting of national policy for energy in the last eight years. The Administration's benign neglect of the oil sector remained undisturbed until the crude price increases of this very political election year.

The fact of the matter is that the Northeast fuel oil market cannot be changed either by chronic releases of the SPR, nor by the creation of additional reserves, as is now being proposed by the Administration. To change the Northeast's exceptional over-reliance on fuel oil for heating, action will be needed, at a structural level, and through determined Federal and State policy to change the fundamentals of that dependence. For the immediate term, the more effective means of getting more supplies to the Northeast for the winter is another blanket Jones act waiver, so that the ample supplies now in the U.S. Gulf Coast, can be moved economically to the Northeast. For the longer term, the region's political leaders should look for solutions that do not shift the cost of their problems to the U.S. taxpayer. These include the construction of a state-of-the-art refinery in New England, expansion of the natural gas distribution system to accommodate more gas imports from the newly-developed field of maritime Canada, and proper economic incentives to encourage dual fuel capacity.

We are not a nation devoid of energy policy choices. But we do tend to avoid hard decisions on matters of crude oil supply and demand. The National Energy Strategy, that I had the privilege of issuing in 1990, forecasts, as closely as it is feasible to do, the supply and demand equation that we have reached today. I warned then and I warn now that without effective policy measures to reverse the trend we are on, we will revisit the issue of high and volatile energy prices henceforth and forevermore. We cannot change the fundamentals of the oil market by the expediency of the SPR or by building regional product stockpiles, anymore than we can change the fundamentals of the gas market by getting into the business of a Federal gas storage; nor can we do so by building Federal powerplants to mitigate some seasonally high prices of electricity. On the other hand, we will change the fundamentals of the energy market by fostering increases in domestic production, deploying technology that reduces demand for fossil fuels, and by getting the Federal Government out of the price fixing business.

Let me state unequivocally, how inappropriate I believe the role of government is in what is generally considered a highly competitive oil market. I read the Energy Policy and Conservation Act of 1975 at its wise face value. And that is that the SPR, which not incidentally was built and filled entirely during the Reagan and Bush Administrations, was created "to diminish vulnerability of the United States to the effects of a severe energy supply interruption." The Act also provides authority under which the United States may carry out its obligations under the International Energy Program. All of us in this room, and previous and current members of this Committee have repeatedly debated the criteria for use of the Reserve, even as we have agreed on avoiding its use principally for the purpose of affecting prices in the marketplace.

I am persuaded that the Administration's release of SPR oil in this instance was used, as feared by Treasury Secretary Summers in his September 13th memorandum to the President, principally for the purpose of affecting prices in the marketplace. I consider not credible the Administration's recourse to the fig leaf of low fuel oil inventories as rationale for the action. In any case, even if worries about low fuel oil inventories were true, there is little the Administration could do to precisely direct SPR oil towards fuel oil production. Indeed, the award of SPR oil contracts to traders devoid of experience in handling physical supplies of oil has severed whatever link there might have been between SPR oil availability and fuel oil production for this coming winter. As a matter of fact, the Administration's election year intervention in the oil market is likely to produce no benefits at all beyond a transitory, entirely superficial shadow on prices. But it will set a terrible precedent for future SPR policy.

Mr. Chairman, the energy sector is unforgiving because it adheres to fundamentals of supply and demand and price, and is immune to political expediency. Only in rare times since the first energy crisis of 1973, has this Nation taken the hard decisions that are the emblem of good policy. The last such time was in 1992 when very strong bipartisan leadership produced the Energy Policy Act. Even then, some decisions proved too difficult to make, even as the consequences of inaction intensify. We have, Mr. Chairman, a second, untapped and unused SPR in the form of oil that lies buried within the Arctic National Wildlife Reserve (ANWR) That oil can be produced with minimal impact on very small acreage. An increase in U.S. supplies of oil, is in my view essential to the achievement of a new equilibrium in U.S. energy policy... but not solely. We need robust diplomacy to deal with OPEC. We need effective investments in new technology. And most of all, we need leadership to avoid exposing ourselves repetitively to circumstances exemplified by this needless regional dilemma.

Mr. BARR. Thank you, Admiral.

The Chair would ask a couple of questions at this time of Admiral Watkins.

What did you think of the testimony from the Department of Energy earlier? Did you hear it?

Mr. WATKINS. I thought it was in line with the normal rules of engagement for a rather low level official to be placed in the position he was placed in. We should have had Secretary Richardson here to answer the questions. These are all political issues, and very important ones. I am sad to see them send up a perfectly good man. I understand he was a former staff person for Senator Byrd. He was a political appointee converted over into the SES force. It is unfair to send him up here, and I don't think you got all the answers you need to have.

I don't agree with someone on this side of the aisle that said this was not an important hearing. This is an extremely important hearing. It is another touchstone in the inadequacy of our attention to energy policy in this country, and it is going to get worse. If we think it is a problem now in the northeast, wait until the price of natural gas begins to go up, with our inadequate supplies. Do we want to have a strategic gas reserve? Why don't we start getting the billions of cubic feet we need now and put it somewhere in the Midwest where the poor Midwest people are going to pay high prices, even in the low economic region in the Midwest. Why should we go to the northeast only?

So what are we talking about here? This is, I think, an extremely important hearing, and it tells us how inadequate we are in our address of oil and gas issues which are the reality of today's transportation sector.

Mr. BARR. I think that most of the members of the committee would agree with you, and I think this is one time where the members of this committee have, in fact, asked the right questions very early in the process, and in some cases, didn't get answers, and in some cases, got answers that were inaccurate and in other cases, quite honestly, got answers that were truthful but at odds with the administration's decision ultimately.

Mr. BARTON. Will the gentleman yield briefly?

Mr. BARR. I will yield to the chairman.

Mr. BARTON. We would have held hearings on the release of the SPR much earlier if not for the fact that the Secretary of Energy told me twice that he had no intention of doing it. We were told that it was not going to happen, so I didn't see a reason to hold

a hearing on something that wasn't going to happen. So we have had to play catch-up because they made an internal decision that they didn't vet with the Congress that they weren't going to do that.

Mr. WATKINS. You weren't able to transmit that thought, though, to Mr. Markey, obviously.

Mr. BARTON. Well, I will keep working on Mr. Markey.

Mr. BURR. I feel confident as time goes on and we get into the annual discussion of the Tennessee Valley Authority and the marketing agencies that Mr. Markey will show his objection to the Federal presence, and clearly that is at odds with his belief that we have to come to the rescue of the fuel oil users in New England.

And let me say, I think we are doing the right thing, based upon the circumstances that exist right now, not necessarily with the sale of SPR, but with the attempt to make sure that adequate inventories are there. The question is, why were we asleep as this process happened, because most members of the committee have seen the deterioration over the years?

Mr. WATKINS. Well, Mr. Kripowicz testified that he has known this for a year. Well, we didn't know it for a year in 1990 when we came to the table, because we weren't attentive to this, and it was John Dingell, who was then chairman of the full committee, who sent Dingell-grams to me daily on this issue, and accused us of not doing our job on heating oil in the northeast.

Well, by God, we went to battle stations on it and we did some hard work, and we brought all of these energy reps and the northeastern Governors into town, and we brought the futures market people down and we said look, this is the situation, this is what we can do with the Jones Act, this is what can work together on and solve the problem, and we solved the problem. We didn't go to the SPR as an alternative.

My problem here with this is not so much misuse of the SPR, but what did you do ahead of time, Mr. President, to address the issues that you could have addressed and maybe solved this problem without making it a big political issue? He didn't do anything that I could see. I didn't hear one thing today that said that they went for a waiver to the Jones Act, which we did, and we got right away and we began to divert tankers headed for Western Europe with heating oil on board to the northeast ports.

Now, I understand that there are maybe tens of millions of barrels of heating oil that can't be moved in non-U.S. flag areas sitting there in the Gulf Coast today, or in the refineries ready to roll. Why don't we move them out? I think your initiation of this bill is very important, but why does Congress have to do that? Why didn't the administration do that as a first choice? Why did they go to the SPR, which is a very complex issue, and it certainly doesn't meet the intent of the law.

Mr. BURR. I yield to the chairman.

Mr. BARTON. Admiral Watkins, as the former Secretary of Energy, do you share the position that the current administration does about the swap provision in the SPR? They have hung their entire legal argument on doing this, on the fact that they have the ability under, really, what I view as an operational title of the Act,

to swap for short-term operational ability, that they can now swap long-term to get more oil in the reserve.

Do you share their view?

Mr. WATKINS. Absolutely not. I think it is the most thinly veiled argument I have heard.

If you use the Reserve for immediate disruptions in the United States where you share with the oil industry, hey, I have a problem in my refineries, I have a problem in my industry, I need help right now, you will get it back next month. That is a different story to me than what we have done in this case. I do not share it. I think it is one of the most convoluted legal, technical, legal go-arounds of the intent of the law that I have ever seen.

I have to give them great credit. I have never seen such a carefully orchestrated end-around to the intent of the law. I think they should get an A for that. Absolutely brilliant, the way they did it.

An exchange? What are we talking about here? My feeling is that this is not the time you make the exchange. There may be some reasons for doing it, but this wasn't one of them.

Mr. BARTON. Thank you.

Mr. BURR. The Chair recognizes the gentleman from Texas, Mr. Green.

Mr. GREEN. Thank you, Mr. Chairman. I appreciate the courtesies of our—of the Chair and the ranking member. I am not on the Energy and Power Subcommittee, but coming from Houston, obviously I have a great interest in this committee, and maybe sometime I will have enough seniority to use to get on the subcommittee.

Admiral, let me ask, because I have been concerned not just in the last 8 years, but for a number of years, about the lack of an energy policy in our country, that really the last energy policy we had was President Carter, and I disagreed with that when I was in the legislature in Texas.

What should Congress have been doing the last 7 or 8 years, to promote an energy policy? Because we haven't been that active either on the House side, or the Senate side.

Mr. WATKINS. No, I think it hasn't done anything. If you decide that advocacy is the way to run an energy policy in the country, you wait for crises and you make decisions, which are probably totally unintegrated overall. When we built the energy strategy, we did it in concert with members of both the House and the Senate, as well as the industry, that we could really carry it out. We went to outside analysts to look at our models to make sure that we were reasonable. The Office of Technology Assessment here in the Congress agreed that they were reasonable assessments of the projected inventories and things. We did all of that. We set up a mechanism within the Information Energy Agency of the Department of Energy to continue this modeling effort with the models then approved over time and about biennially, adjust the strategies and, if necessary, adjust the law to meet the changing times, both in technology and other things. That has not been done at all, and nobody has raised any question about it. I don't know why.

I blame maybe this committee as well as the committee in the Senate to disallow the Department of Energy not to follow it, and if they are not going to follow it, they better come up with good rea-

son not to follow the Energy Act of 1992 and carry out its provisions and upgrade it and demand a real energy strategy, not one that is advocacy-only on one side of the equation. You can't do it that way.

We don't like nuclear anymore because of waste, we don't like hydro because of fish ladders, we don't like fossil energy because of global warming. What do we like? We love jobs and we love GNP directly connected with electrical output. What is going on? In our strategy, we were actually getting less and less dependent on foreign imports, if we did what we said we would do, but we didn't do that.

Mr. GREEN. Admiral, I agree, because this Congress hasn't done anything really since the Energy Policy Act of 1992, is that correct?

Mr. WATKINS. That is correct, in my opinion.

Mr. GREEN. Let me ask you a question about—I would like to get your thoughts on this, because SPR, granted it was for strategic issues and really for embargoes, but it is being used now to try and have some flexibility in the market, but in 1996, Congress actually suggested we sell 20 million barrels of oil for deficit reduction purposes. Could you comment on that?

Mr. WATKINS. Yes. I think it was a bad idea. I think the Congress shouldn't have done that. Here we are today accusing the administration of misusing the Strategic Petroleum Reserve and we did it then. We can't be for free markets and then for market interference. It is incredible to me how we can speak out of both sides of our mouths.

Mr. GREEN. Well, let me follow up on that. I agree. In fact, again, it seems strange that we would try and sell oil when it is \$12 a barrel that we probably bought for \$27 a barrel. The whole point should be that when the oil is cheap, we should use the—we should stock up to prepare for the times when we need it. I also don't know if we have a free market, again, simply because our markets are not controlled by our government, we hope, but it is controlled by other governments, whether it is Venezuela, whether it is Saudi Arabia, whether it is OPEC, a coalition of governments; so to say we actually have a free market, it is really controlled by other governments other than our own.

Could you comment on that?

Mr. WATKINS. That is true, I agree with that. But on the other hand, we are going to the bargaining table with a tin cup running around to the OPEC cartel saying please increase your production, and the next move we make is a \$30 million drawdown on the Strategic Petroleum Reserve. If I were them, I would just cut back 1 million barrels a day for 30 days. I don't understand what we are doing is all I am saying, and it is not integrated with any other element of what we thought was a good national energy policy in 1992 and that should have been continued, and maybe, maybe, we would have gone on today to find out that what we were doing here in setting policy on one side of the equation only was in the long-range bad interest of the United States.

Mr. GREEN. Well, I agree, we should do more. In fact, that is why hopefully this committee in the next session of Congress, and we should have done it for the last 8 years, to really develop a national energy policy.

But the other interest I have is that I have seen the price of oil in Houston, Texas, the price of gas at the pump actually go from, at one time it was inching from \$1.45 to \$1.50 and now you can buy it this weekend in Houston for \$1.32. So granted, it is short-term relief and we need to look for long-term relief.

Mr. WATKINS. We need to get on with long-term relief. In my opinion, there isn't any short-term relief except to do the kinds of things I laid out in my testimony here today, and my feeling is to use something to interfere with the market prices when we are down to 175th of the input internationally is a mistake. We don't have the leverage, and we need to get the leverage back, and we need to go into alternatives that we have not, in my opinion, aggressively pursued.

We don't mind having the Gulf Coast do the drilling off their shores, but we disallow the incredible gas reserve that is sitting off the East Coast, the West Coast, and the crude oil that is sitting up in Alaska.

Mr. GREEN. Well, Admiral Watkins, you are preaching to the choir.

Mr. WATKINS. I don't get that. I don't understand that. We are willing to use the refineries in the south to send fuel oil to the northeast, but the northeast is so pristine and so arrogant that they will not build a state-of-the-art, prestigious refinery today to do their job.

So some of those things have to be ironed out. Those are political issues, those are not technical issues.

So I don't know how you come to grips with it up here. When we went through that act in 1992, it was one of the most contentious acts. The reason we got it passed, frankly, is we left CAFE standards alone for John Dingell, and that is how we got it passed. Sometimes you have to compromise on those things and do it. And we did it and it didn't defy the principles we set up in the energy policy. But it was never continued and we just dropped it, and here we are in the same mess we were in 8 years ago.

Mr. GREEN. Mr. Chairman, just in response, I go offshore in my district and I see the success we are having in offshore deep water, Gulf of Mexico. We are drilling and we are being successful and environmentally correct. In fact, our fishermen will tell you they would rather fish around a platform than anywhere else.

Mr. WATKINS. I have checked out of those platforms and you can't do it because of environmental considerations because they are one of the greatest fish habitats in the world.

Mr. GREEN. In fact, in the early part of this decade, we were actually destroying some of those platforms so they could be reached off the coast for that habitat, but there is a way you can drill offshore successfully and environmentally safe. Again, sometimes up here the only States that do it are Alaska, Texas, Louisiana and Mississippi, but no one else is willing to tap their reserves.

Thank you, Mr. Chairman.

Mr. SHIMKUS [presiding]. Thank you.

To the panel I understand we are going to finish with you, Admiral Watkins, and then we will go to opening statements. So just a few comments, if I may, and I will take my 5 minutes and then we will dismiss you, Admiral.

You said during the first—actually, the second panel, and under—was it your impression that the International Energy Association's guidelines for on-hand storage in case of emergency was solely based upon a SPR, or should that, as was testified, taken—

Mr. WATKINS. That is some legal interpretation that has come out. We never discussed anything like that when I was Secretary of Energy. It just never came up as an issue to misuse it in that form. I don't say that, you know, you can't go into the technical aspects of the law and jesuitically move this thing around so that you can come out with something that just makes sense. I think that is what was done here. I don't think it was ever the intent, particularly for this large a drawdown. For some of the lesser ones that we heard about for production problems here of an immediate nature, I think something like that could be justified, providing you notify the Congress, providing you notify your international partners of what you are doing so that they are not misled as to whether or not you are trying to interfere with market prices.

Mr. SHIMKUS. Under the International Agency's guidelines, there is supposed to be coordination between the signatures on a release. Did that happen in 1991? Do you think that happened during this most recent release?

Mr. WATKINS. I know it happened in 1991. I was involved directly in it. I was in direct communications with the Saudi Minister of Energy on private circuits, monitoring every single event in the Gulf at the time through his contact with the other Arab nations; I was in communication with the Paris group, the IEA in Paris, telling them exactly what we were doing, encouraging them to make sure that those that did have reserves were ready to draw down, as we would. That means you have to go out and run a drill, and we ran a drill in October 1990, before the war, with great discussion in the Cabinet as to whether or not we were going to interfere with prices, even at 4 million barrels coming out for testing purposes, testing the bidding process, prequalifying bidders, getting all ready to go.

But the signal we sent, and the NEA agreed with us, that we were sending a signal to Saddam Hussein that we were serious internationally, and when necessary, the international inventories, which were significant when you add them all up, would be a strong deterrent for him to think that he could control the economies of the world by attacking Kuwait and Saudi Arabia without us getting involved.

So my feeling is that those were all legitimate uses, and I think this is an illegitimate use of the reserve, and when there are alternatives available.

So we did it for other purposes. We did it for price control, and it wasn't that long lasting, as you saw, because the spooking of the commodities market by the Middle East crisis is far greater than anything we can pump out of the little reserve we have. So it is nonsense to use the rationale that I have heard here this morning to try to justify what we are doing. I don't get it. It is certainly not to fill the reserve at this price for oil. Why didn't we buy it when we were at \$10 a barrel and put in the 750 million barrels to fill the capacity?

Those are the kinds of questions that I think don't get aired very well. The press doesn't pick them up, nobody takes it on, and so we see drifting into this inadequate future that we now have proven to be faulty, again, because we haven't kept up pace.

Mr. SHIMKUS. As you have observed through your time testifying before us and my background, an overall national energy policy is a critical component from our marginal wells, which I have an abundance of in my district, to nuclear, coal and all of those aspects.

I am just going to briefly get off on the petroleum reserve for 1 second and ask you if you are familiar with the uranium processing plant in Metropolis, Illinois, and the fact that it is 90 days short of closure because of the U.S. purchasing of reprocessed uranium from the Soviet Union, which is now, in essence, a subsidized competitor to a government-sponsored corporation, thus endangering I think another aspect of our national energy policy and our national security, because as with petroleum, now we are losing a refinery, in essence, on uranium. Can you comment on that?

Mr. WATKINS. Well, I can't comment specifically about the installation in Illinois. Obviously, I am very upset that the Nation, which has technical solutions to the various waste and other problems associated with nuclear power operations, is basically throwing this option out the window. We haven't built a new nuclear power plant, as you know, in 20 years, and yet on the table we have completely researched and prelicensed inherently safe reactors. We know how to bury the waste, but nobody wants it in their backyard. We are quite willing to supply a reactor to North Korea, but we won't supply one to ourselves. I mean, you tell me the logic and the rationale for all that. I can't find it. I think 10 years from now we will wake up and say we can't meet air quality standards and why don't we reopen the issue of nuclear. We will surely do that.

As a matter of fact, the way the utility commissions are going in the various States right now under the deregulation, the rate base is picking up the stranded cost investments of those nuclear plants and you are going to see far fewer go down of the existing plants, but we are going to end up 20 years from now with very old plants.

So we need to get on with a new nuclear power option and get on with it and demonstrate to the world that we know how to bury this stuff, and we need to reopen the various issues of where we can bury this waste in the stable clays of the earth which are existent all over the earth. It doesn't have to be in Nevada, it can be in other places, and we ought to get on with it and do the research work and really boost up the contribution we make so that we can cut back on coal, we can cut back on the fossil fuels.

But absent that, we are going to continue to have these kinds of hearings about every other year, and it is not going to be any better in the northeast, I can tell you that right now, unless they start converting over to gas and begin to make contracts with their Canadian partners in their northeast Governor's councils. They ought to get on with it.

Mr. SHIMKUS. We are still going to be on schedule to get you released by 1 but the ranking member would like to ask a follow-up question.

Mr. BOUCHER. Admiral Watkins, thank you for joining us here today. I can't resist, hearing you mention coal, asking you this question. In my congressional district, we mine all of Virginia's coal and we are very interested in seeing coal take a higher posture in the fuel that is used for electricity generation.

Do you have any advice for us on what we can do to achieve that goal?

Mr. WATKINS. I think we are moving in the right direction with clean coal technology. I was on the board of directors of a major utility in the country. Under the deregulation process, we bought up some very poorly run coal-fired plants. We are putting in the scrubbers in those plants. That was part of the deal in the merger I think we are doing a wonderful job there in the coal industry, and I would never want to throw that out. After all, we are small potatoes in the world of indigenous supplies of coal. I mean what about India and China? They are emerging. They are excluded from some of these Kyoto agreements and other things because of coal, and we are going to penalize ourselves? That is nuts.

My feeling is that coal today is about 57 percent of the power generation in the country; it was only about 53 when I was Secretary of Energy. So by environmental standards, we have gone in the wrong direction, and I haven't heard a peep out of them. What is going on?

My feeling is that coal will continue to play the major role in power production in this country, the major role in GNP growth, because you need that energy, and the only thing we have to do is make sure the technologies are maintained and continue to put the money in to clean coal technology as time goes on, that is better than what we have today.

Mr. BOUCHER. I have heard it said by some utilities that one of the reasons they don't rely on coal for their due generating capacity is because it is so difficult to get permits. Is there something that we can do to facilitate the permit-granting process that would perhaps stimulate electric utilities to use coal?

Mr. WATKINS. I think this committee would do one of the great services and reenergize interest in the energy strategy by seeing the degree to which regulatory authority has been imposed on a whole host of energy sources, including hydro. Nobody wants to renew a hydro plant today because the agony and pain to go through FERC is 7 years at great expense.

I don't agree with that labyrinth that people have to go through. There should be a complete review of the degree to which we impose these problems on ourselves for political reasons at the time they are passed, and then we leave them there forever. That is what we have done in most of these cases, and I would hope that would be a part of the attack of this committee on an energy policy for the future, to get on what have we done to impede our own energy policy. We have done a lot, and we should not let those things stand forever. We should be reviewing those things at least every 5 years. We ought to be legislating again and keeping these things dynamic.

Coal was getting a bad name. It doesn't get a bad name anymore because it should not have a bad name. There is no reason not to have clean coal technologies applied. And given the standards and

all of the brouhaha on acid rain, that went down the tubes on the analysis. It wasn't really there except in selected cases. We have overemphasized one side of the advocacy equation called environmentalists, and we need to get in balance with GNP, economy and so forth because they are the ones that want jobs, too. They want GNP growth so we can't have it both ways. We need to come together as we did in 1992 and put this thing in a package that makes some sense, and that would include the northeast and what they ought to be doing. Use the bully pulpit. You can't interfere with the market, but you can influence that market by encouraging those northeast Governors to come to the table and be reasonable as other states have been on who generates the energy and refines oil, and come on board with the rest of us, don't stand out there as if you are something unique and special in this country. Maybe you are, but let's be equitable across the board.

Mr. BOUCHER. Thank you very much for your views. Thank you, Mr. Chairman.

Mr. BARTON. Admiral, we are going to let you go.

Mr. WATKINS. I have some strong views on this that I will talk to you later on.

Mr. BARTON. We want to hear the strong views now that we have heard the mild views. We are now going to continue with this panel. Hopefully we will get all of your testimony in. We have at least an hour before the next vote. We will start with Mr. Martin and go to Mr. Wolkoff, Mr. Surma, Mr. Manzoni and then Mr. Boles.

STATEMENT OF WILLIAM F. MARTIN

Mr. MARTIN. Thank you, Mr. Chairman. Much of what I was going to say has been said by Admiral Watkins. He is a hard act to follow.

Let me say, I had an interesting experience from 1977 to 1981 to be the assistant to the director of the International Energy Agency, and I would like my remarks to look at the international setting. I believe it is folly to think that 30 million barrels of oil is going to affect a world oil market of 75 million barrels a day. If people are concerned about price, they would have coordinated actions within the IEA. I think we are headed toward a time when the IEA and stock policy is going to become much more important, especially as Asian demand increases on the Persian Gulf. It is likely we will have a crisis within the next 5 years. That is why having this hearing is important to review why we have the SPR and why it needs to be coordinated with our European and Japanese markets.

In 1974 in the first oil embargo, the IEA was formed. The mechanism was a sharing system. If oil markets hit a 7 percent shortfall, we would share oil. But when we came up to the Iranian revolution in 1979, there was only a 2 percentage dropoff but the oil price almost tripled. Why? Because companies were like auto users: They topped off their tank. If you fear a crisis, you add to your stocks. So we exaggerated the oil crisis, and we all paid for it. When the Iran-Iraq War started in 1981-1982, and this was at the beginning of the Reagan Administration, it was decided that rather than shoot ourselves in the foot collectively again, all of our countries,

we would actually draw down stocks, and we did and countries were penalized if they were going to build stocks.

Following that, in the Reagan Administration we made an effort to build the Strategic Petroleum Reserve, but the key was coordination with our allies because when we put a barrel in Louisiana, that is for the everybody-in-the-world oil market. We also figured out if we were the only ones building, we were going to be subsidizing everybody else. I met with the Vice Minister of Amity, Mr. Merota, and said Japan should build stocks and they did. The Germans built stocks. Some have as was raised today, the right to urge private stock use and that counts within the IEA definition. But the reality is we built up stocks, so when Secretary Watkins was able to confront the Gulf War, we had an effective deterrent collectively.

Let me also say that Ronald Reagan also built up the defensive capabilities in the friendly Arab states, so when Secretary Watkins came in, he had a strong defense and not only a coalition, we always think of the coalition of people fighting the war, Secretary Watkins also had a coalition of consuming countries behind him with a large SPR.

So when I saw that the administration was using 30 million barrels for what, my first question was, well, have you talked to the allies? What are they saying about this? Of course, they are delighted because we are putting 30 million more barrels of oil on the market. They are not going to complain. They must be thinking in London and Paris what are these people doing. They understand what the present administration is doing, and that is why I have relabeled in the title of my testimony, "SPR or PR?" I really do think that it is PR. I don't doubt that the administration is motivated, as Secretary Richardson was last year, to go around the world and try to get production up because we don't want to have wild swings in stocks, but where was Secretary Richardson when the price was \$10 per barrel in Oklahoma and Texas?

I would urge, Mr. Chairman, and I would suggest that next year's G 7 summit in June is going to be the energy summit. I predict that right now. There will be a lot of measures out on the table, what should we do because the Italians are chairing it, and they are 80 percent dependent on oil for their total energy. It is like the Venice Summit of 1980.

So I would like to see the next President look not only at a national energy policy, but I would like to see him go prepared to Italy, and part of that may be what this committee has been talking about for several months now, a credible national energy policy. That would be nice thing for the next President to take to the table.

I also suggest that the committee delve into what are the criteria for using the SPR and indeed, how should we coordinate it with our IEA partners? Thank you very much.

[The prepared statement of William F. Martin follows:]

PREPARED STATEMENT OF WILLIAM F. MARTIN,¹ FORMER DEPUTY SECRETARY OF ENERGY

Good morning, Mr. Chairman. I recently spent a year co-authoring a report entitled *Maintaining Energy Security in a Global Context* for the Trilateral Commission. My co-authors, former IEA Director Helga Steeg and Ambassador Ryukichi Imai of Japan, interviewed over 100 senior government officials and researchers on energy security and our report in 1977 has been published in five languages. We specifically addressed the important issue of strategic stocks and their coordination during a crisis.

The Strategic Petroleum Reserve (SPR) of the United States represents the largest and most important reserve among industrialized countries. As such, the United States has the key leadership role in deciding when to use stocks and coordinating international responses to energy emergencies. It is for this reason that the Administration's recent decision to release 30 million barrels from the reserve should be considered as more than just a domestic policy option to offset price increases. In fact, the SPR must be viewed as a mechanism that is at the heart of US national security policy.

I would like to make six observations.

1. The SPR was designed to be the main element of U.S. response to a serious oil disruption threatening U.S. national security.

The SPR is not a TPR (tactical strategic reserve); nor is it a PPR (political petroleum reserve); nor is it a PR reserve. It is a *strategic* petroleum reserve designed to be used in serious national emergencies. It was also built with an eye towards coordination with other member countries of the International Energy Agency (IEA). My impression is that the Administration was genuinely concerned about higher oil prices, but their effort to tap the SPR—even through a swap deal—appears a bit more than opportunistic, in part because it has not been accompanied by a cooperative effort to coordinate an international stock draw. If they intended to have an impact on price, then an international stock draw—through the IEA—would have been a far more effective strategy. As it stands now, the U.S. has drawn the SPR unilaterally for the benefit of all nations who use oil.

2. Release of SPR will have little or no impact on oil prices.

The price of crude oil continues to fluctuate in the \$30-37/barrel range following the Administration's announcement that it would tap the SPR. The reason is simple. The impact of adding 30 million barrels to oil markets is negligible, representing less than half a day of global oil consumption (total daily global demand is approximately 75 million barrels). The measuring stick for potential impact of such a release should not be just U.S. oil consumption, but rather international oil consumption because we are part of an integrated, global market. While the Administration's release of stocks will reduce oil imports a bit, the reality is that a European or East Asian country could easily import that amount of oil and put it into their stocks—negating the impact of the SPR release. Other experts have cautioned that it will also have little impact on relieving the heating oil crisis in the Northeast. A 30 million-barrel release does not directly translate into heating oil stocks for these states. In fact, the refined products resulting from the release will be sold where they fetch the highest price. There have been recent reports of some U.S. refiners shipping heating oil to Europe where prices are even higher than in the domestic market.

3. The "founders" of the SPR viewed the SPR as a national security asset to be enhanced and coordinated with stocks in other nations.

Following the Arab embargo of the U.S. in 1973, Henry Kissinger urged the creation of the International Energy Agency. The IEA was founded upon the principle that countries must build 90 days of stocks. In the event of a 7 percent shortfall, member governments were obligated to share oil with other countries.

However, in 1979 the Iranian revolution resulted in only a 2 percent shortfall, far below the IEA trigger of 7 percent and caused prices to more than double to over \$40 a barrel. This contributed to one of the most significant economic recessions of the last three decades. What happened? Instead of lowering stocks, countries built stocks—putting added pressure on markets. There was a key lesson here—countries, like auto owners, "topped off their tanks" creating added pressure on prices.

¹ William F. Martin is Chairman of the Energy Security Group of the Council on Foreign Relations. He is a former Deputy Secretary of Energy and Executive Secretary of the National Security Council. During the second oil crisis, Mr. Martin was Special Assistant to the Executive Director of the International Energy Agency in Paris.

In 1981 when the Iran-Iraq War caused more market insecurity, the IEA members learned a lesson from history and agreed to collectively lower stocks. Rather than build stocks rapidly, there was sufficient international will power to lower stocks together. This effort dampened upward price pressure and in fact pushed prices down. I would like to point out that a bipartisan effort helped this process. Outgoing officials of the Carter Administration and the incoming officials of the Reagan team both saw the value of building and coordinating stocks.

Mr. Chairman, you will recall that the Iran-Iraq War intensified during the period 1984-85 and President Reagan took active measures to urge all countries to build their stocks and to clarify rules for their use—the key of which was coordinated stock draw. Many countries, including Japan and Germany, built stocks at our urging. The United States actively sought a 600 million-barrel SPR and we agreed in 1985 on a plan to coordinate stocks internationally in the event of a disruption. In tandem with this effort we helped expand the defense capabilities of the friendly Arab countries in the event that war might spread into Kuwait and Saudi Arabia.

The next crisis was triggered by the Gulf War. President Bush and Energy Secretary Admiral Watkins had the advantage of a well-stocked SPR, available for use to impact and stabilize the world oil situation. They also benefited from Reagan Administration efforts to increase the defensive capabilities of friendly Arab states. Secretary Watkins and National Security Advisor Scowcroft and their staffs worked very hard within the IEA framework to develop a common policy among the IEA countries. The results were commendable. Even though the SPR was only tested—it did serve as an effective deterrent. Our allies appreciated that not only did the U.S. build a coalition force to protect Kuwait—we also build a coalition of countries within the IEA to coordinate emergency release of oil stocks.

The point of my historical observations is that both Democratic and Republican Administrations have been hesitant to use the SPR. Like a strong military, the SPR was seen primarily as a deterrent, a mechanism to be used only as a last resort and when national economic security is severely threatened.

4. The Strategic Petroleum Reserve can help relieve physical shortage and moderate prices—but it should be used in coordination with the stocks of other nations.

Let me give a definition of when and how the SPR should be used. The SPR is America's first line of defense against oil disruptions. It is a national treasure which when coupled with the effective use of stocks in other countries can calm and bring reassurance to troubled oil markets. The SPR can be used to moderate prices when it threatens our economies and it can be used to help relieve a physical shortage. But it should not be triggered in isolation of international cooperation with the IEA countries.

If the Middle East were to go up in flames next week and oil markets were disrupted then I would be quick to call for a stock draw both in the U.S. and within the IEA. But I do not think the present SPR swap was necessary and I do not believe it will be effective. Nor do I think that Secretary Richardson's efforts to pressure producer countries earlier this year was particularly effective in gaining their cooperation. Again, let me stress that the motivation may have been commendable, but the signal this Administration has been sending to both consuming countries and producing countries is that the U.S. will act unilaterally in matters of energy security. The SPR release undermines our international leadership and credibility.

5. The next President should focus on national energy policy as a high priority

The reality today is that oil markets are on the razor's edge—inventories are low; demand is increasing—and it may take years for new supplies to be on the market. Many experts agree, however, that current oil prices are sufficient to encourage a new wave of resource development, especially given the pace of technological developments. But much of that supply will not be on the market for at least three to five years and we can expect some bumps in the road until then.

As the members of this committee know full well, the current situation is a reminder that we must accelerate our efforts to put in place a national energy security policy that emphasizes the development of our domestic resources. We should (1) allow greater access for oil and gas exploration on Federal lands; (2) fully tap the potential for greater use of natural gas, by supporting R&D for new gas using technologies and enabling an expansion of natural gas infrastructure; (3) encourage the deployment of clean coal technologies; (4) relicense hydro plants (5) encourage continued R&D for renewable sources and energy efficiency, and; (6) maintain our nuclear power capability through life extension of our nuclear plants.

6. Any solution to the present energy situation must be an international one.

I would like to recommend that we also pursue an international strategy to calm markets in the next few months within the framework of the Head-of-State G-7 summit in Italy next June and the IEA and OECD Ministerial meetings in May.

I expect that the next G-7 summit will focus on energy and the next President should be in a position to show leadership, listen to the energy challenges confronting other nations, and work to collectively forge an international energy policy. In addition to taking a strong U.S. domestic energy policy to the table, the President should use the present situation to (1) urge all countries, including the U.S., to evaluate their stock positions and possibly increase the size of those reserves given the likelihood of growing oil import dependence in the future; (2) closely monitor current oil market developments—supply and demand—throughout the coming critical winter months; (3) evaluate alternative international strategies for releasing some oil from stocks should the situation warrant market intervention; (4) continue bilateral discussions with producer countries to consider their short and long-term interests, and; (5) be prepared to respond to any real oil supply emergencies arising out of the current troubled Middle East situation.

Mr. Chairman, we are fortunate that this Committee has been holding hearings throughout the last few months to address U.S. energy policy. This gives the next Administration an opportunity to move quickly on energy policy. A credible national energy policy will allow the President to demonstrate real leadership at the G-7 summit in Italy next June. U.S. leadership to forge a sound international energy policy with our Japanese and European colleagues will ultimately benefit U.S. consumers and help relieve our growing dependence on oil imports from the volatile Persian Gulf. Thank you.

Mr. BARTON. I agree with you. We need to do that. We appreciate your waiting, all of the panel. This is no fun to sit for 4 hours, and I apologize for that.

We are now going to hear from Mr. Wolkoff who is with the New York Mercantile Exchange. We would like to hear your comments. We put your statement in the record and we give you at least 5 minutes to summarize.

STATEMENT OF NEAL L. WOLKOFF

Mr. WOLKOFF. Thank you for the invitation to be here today. Just a couple of comments, a few words describing NYMEX. I would like to lead off by saying that NYMEX is a regulated entity. It is a nonpartisan organization. We are price neutral. That means that our policies do not favor either low or high prices. Our goal is to represent further competitive markets with fair and rational pricing.

Mr. BARTON. We will stipulate that you are neutral.

Mr. WOLKOFF. The relevance to this hearing is that NYMEX is the price determination forum for benchmark contracts, crude oil, heating oil and natural gas. Being a benchmark means that the prices established on NYMEX are accepted as the leading price reference by far for the purchase and sale of oil and gas on the commercial wholesale market.

Quickly, getting into the couple of SPR issues, NYMEX's views on the release of oil from the SPR is consistent with NYMEX's view, which has been stated many times over the years, that governmental intrusion into the energy markets must be predictable and subject to specific, clearly identified objective standards. NYMEX is not opposed to a strategic petroleum reserve, although its use would always be a governmental intrusion into the marketplace. Instead, we are opposed to a sudden, unpredictable use of a SPR because such a use cannot be planned for in advance, it cre-

ates market volatility and incentive for future conduct, which is not desired.

There are two specific items I would like to amplify. The first is the impact of an SPR release on supplies and prices later next year is a concern. The SPR swap release appears to have lowered prices temporarily. The government's action coincided with a price drop of approximately \$1 per barrel in the front month, that being November crude oil. I provided some charts which show the apparent effect of the SPR announcement and subsequent bidding process on short-term prices. They show that the action did little to change the market's fundamental sentiment on oil prices going forward, that is, prices are expected to decline according to the forward price curve.

As a price lowering action, the SPR release appears to have worked in the short term. Albeit its effect may be overwhelmed by other market factors such as Mideast hostilities. Whatever the effects such a release has on prices this year, the question remains, what impact the government's action will have once the oil is required to be paid back? Will the repayment come at another period of supply tightness and thus exacerbate market conditions later next year? The SPR swap deal provides a temporary inflow of crude oil into the marketplace, but in the longer run it will reduce the supply of oil later on as the obligations of repayment to the SPR come due.

The second point on the SPR issue is the impact on future supply decisions by the companies that supply oil and gas to the public is a concern. The government's release of SPR oil could encourage refiners and suppliers to hold lower inventories, which is clearly an unwanted and unwelcomed outcome. The decision to release can create a concern among the supply and distribution companies of future governmental interference in the marketplace, which might cause financial losses for any inventories being held at the time.

I used my 4 hours in the waiting area somewhat productively. I can illustrate at the time of the SPR release, there were 290 million barrels of crude oil in storage. There are about 110 million barrels of heating oil in storage, and another 200 million barrels of unleaded gasoline. If the SPR release lowered prices by \$1 a barrel, it would have affected a transfer of wealth of \$600 million, simply based on those barrels that we knew of in storage. Many other barrels are contractually owned but not stored, and they would have had their prices affected as well.

It is the concern that this action by the government in transferring wealth from those in the business of supplying the marketplace with oil will, in the future, create a concern that high inventories can have their value again reduced by similar unplanned and unpredictable government action. That is a legitimate concern and one that I am afraid will be with us for the next several years.

Commercial participants in the oil market make supply decisions based on their interpretations of market conditions. There is a market incentive for refiners to make appropriate business decisions. After all, the customer can always do business with another supplier.

To finish, I would say inventory decisions should be left to the marketplaces. Free markets have been a very effective oil policy for

the last 20 years. The marketplace has shown itself to be self-correcting and efficient. The SPR decisions to influence price, ironically, create incentives for refiners and suppliers to hold lower inventories, which ultimately is bad for the consumer. Lower inventories do not provide a buffer against price shocks caused by sudden increases in demand. To the contrary, lower inventories contribute to price spikes.

Thank you.

[The prepared statement of Neal L. Wolkoff follows:]

PREPARED STATEMENT OF NEAL L. WOLKOFF, EXECUTIVE VICE PRESIDENT, NEW YORK MERCANTILE EXCHANGE

My name is Neal Wolkoff. I am the Executive Vice President of the New York Mercantile Exchange ("NYMEX" or the "Exchange"). On behalf of the Exchange, I wish to thank you for the opportunity to participate in today's hearing on the Strategic Petroleum Reserve (SPR).

I. DESCRIPTION OF NYMEX

NYMEX was established in 1872. NYMEX is federally chartered and regulated by the Commodity Futures Trading Commission ("CFTC"), an independent regulatory agency similar in purpose to the Securities and Exchange Commission. NYMEX is the largest physical commodity futures exchange in the world, offering contracts for energy, and base and precious metals. NYMEX is also the largest energy exchange in the world.

Of most relevance to this hearing, NYMEX is the price determination forum for benchmark contracts in crude oil, heating oil, gasoline, and natural gas. Being a "benchmark" means that the prices established on NYMEX are accepted domestically (and in the case of crude oil, internationally, as well) as the leading price reference, by far, for the purchase and sale of oil and gas on the wholesale market.

For essentially two decades, the marketplace has been fortunate to have highly liquid, transparent futures markets for heating oil, gasoline, crude oil, and natural gas to provide a window on the market's actions. Physical supplies of crude oil and refined products are traded on NYMEX in an open, competitive, and regulated marketplace. Each transaction is consummated in a completely visible open outcry auction with an extensive audit trail. Buyers and sellers vying for the best price in a transparent marketplace cannot make a market with tight supply cheap, or a market with abundant supply expensive. However, they can make the pricing fair and rational.

The Exchange pioneered the development of energy futures and options. From a modest 34,000 heating oil contracts traded in 1978, NYMEX energy futures and options volume grew to more than 89 million contracts in 1999 and now includes crude oil, gasoline, natural gas, electricity and propane in addition to heating oil.

II. THE ROLE OF FUTURES MARKETS

Futures markets provide two important economic functions: price transparency (price discovery) and risk shifting (risk management). Both of these functions are mandated by the Commodity Exchange Act, which is the federal statute governing NYMEX and other U.S. commodities exchanges. In addition, NYMEX is under the requirement by statute to further the public interest.

Price transparency is the constant reporting to the world of the prices of actual trades being made at NYMEX. With tens of thousands of energy contracts¹ traded

¹ Futures and Options Contracts

A futures contract is an agreement between two parties for delivery of a particular commodity at a specific time, place and price. Once initiated, a futures contract obligation can be satisfied by either taking an equal and offsetting futures position or by going through the delivery process and taking possession or making delivery of the commodity. The vast majority of market participants opt for the former, and as a result, futures contracts are primarily used as financial rather than physical management tools.

An options contract bestows upon its owner the right, but not the obligation, to buy or sell the underlying futures contract at a specified time and "strike" price. The option to buy is called a "call", and the option to sell is a "put". A major appeal of options is their similarity to term insurance. The option is purchased for a one-time fee called an option premium. Depending on

Continued

daily, each reflecting a binding commitment to make or take delivery of a specific commodity, price information is made available real-time, on a virtually continuous basis over a ticker network.

Risk shifting, in the secure liquid markets that NYMEX provides, allows commercial interests to "hedge" the risk of price fluctuations that could affect profitability and planning of their business operations. For the commercial participant, the result is a form of insurance against the financial adversity that can result from volatile energy prices.

III. NYMEX SERVES A BROAD MARKETPLACE

While the principal market served by NYMEX is composed of those involved in financial risk management, the utility and necessity of its price reference functions are substantially broader, and serve a valuable public purpose by enhancing competition in the marketplace.

NYMEX's markets are widely utilized by all segments of the domestic and international oil and gas industries, and by major banking institutions, among other participants. NYMEX's prices are disseminated to the public in every major industrialized nation on a real time basis. The transparency of NYMEX's prices, and the integrity of its markets, makes NYMEX a benchmark for energy pricing around the country and the world.

On any given day, the NYMEX energy complex averages the trading of approximately 225 million crude oil equivalent barrels per day. That represents nearly 3 times daily world oil production—and 9 times daily OPEC production, with an annual notional value of nearly \$2 trillion.

IV. SPR ISSUES

NYMEX views the release of oil from the SPR consistent with its view stated many times over the years that governmental intrusion into the energy markets must be predictable, and subject to specific, clearly identified objective standards. We are not opposed to a Strategic Petroleum Reserve, although its use would always be a governmental intrusion into the marketplace; instead, we are opposed to sudden, unpredictable use of a Strategic Petroleum Reserve, because such a use cannot be planned for in advance, and creates market volatility and, as described below, incentives for future conduct that is not desired.

A. The Impact of an SPR Release on Future Supplies and Prices Is a Concern

The SPR swap release appears to have temporarily lowered oil prices. The government's action coincided with a price drop of approximately \$1 per barrel in the front month of November crude oil. The accompanying charts graph the apparent effect of the SPR announcement and subsequent bidding process on short term prices.² They also show that the action did little to change the market's fundamental sentiment on oil prices going forward (prices are expected to decline, according to the forward price curve).

As a price lowering action, the SPR release worked in the short term, albeit its effect may become overwhelmed by other market factors, such as Mid-East hostilities. Whatever the effect such a release has on prices this year, the question remains what impact the government's action will have once the oil is required to be paid back. Will the repayment come at another period of supply tightness, and thus exacerbate market conditions later next year? The SPR swap deal provides a tem-

how the market moves, the option may be sold for a profit, exercised, or allowed to expire worthless, with the holder's loss limited to the premium paid.

NYMEX guarantees the financial obligation associated with all contracts open on NYMEX. The strength and liquidity of NYMEX is found in the financial integrity of its clearing system, and its commitment to the provisions of fair and orderly markets. NYMEX has taken strong steps to ensure integrity, including daily price limits, customer margin requirements, speculative position limits, market surveillance and strict financial requirements for all NYMEX members. As the world's largest and most innovative energy futures trading forum, NYMEX offers the experience and the security to help industry manage the global challenges of today's dynamic price realities.

²The price impact of the SPR swap release will be temporary, and will not have much impact in the longer term. Although the immediate impact of the SPR release has been lower prices in the near term by about \$1.00 per barrel, the SPR release has not altered the price curve for oil. The price of oil continues to be in backwardation, a term that means that prompt delivery of oil is priced higher than future delivery. On September 21, one day before the announcement of the SPR swap plan, the backwardation in the crude oil market was \$.59 cents per barrel for November delivery as compared to December. As of October 17, the backwardation continued to be \$.57 for November vs. December delivery.

porary inflow of crude oil to the marketplace, but in the longer run will, in fact, result in a net reduction in the supply of oil as the obligations for repayment to the SPR come due.

B. The Impact on Future Supply Decisions Is a Concern

The government's release of SPR oil could encourage refiners and suppliers to hold lower inventories, which is clearly an unwanted outcome. The decision to release can create a concern among the supply and distribution companies of future governmental interference in the marketplace which might cause financial losses for any inventories being held at that time. Arbitrary, i.e., non-emergency, use of the SPR oil by the government to influence price interferes with the decision-making process, and therefore interferes with the normal marketplace incentives to be reliable and customer-friendly.

Commercial participants in the oil market make supply decisions based upon their interpretations of market conditions. There is a market incentive for refiners and suppliers to make appropriate business decisions that are intended to satisfy customer and consumer needs. After all, like any business, if a refiner or supplier fails to meet its customer's needs, the customer can do business with another supplier.

The various suppliers and refiners of crude oil need to factor in the potential release by government of SPR oil in making an inventory decision, with the end result that the consumer is likely to be the one to suffer. In essence, in a world governed by marketplace consequences, without government intervention using the SPR, a supply decision to carry low inventories can have significant commercial consequences to a refiner's business if his judgment is wrong.

However well meaning, government interference can provide perverse incentives. For example, with a government inventory to fall back on, the SPR actually provides a buffer for the supplier or refiner, allowing him to err on the low side for inventory. If wrong, the SPR will be there to bail him out. In addition, if he chooses to maintain a normal or higher-than-normal inventory to assure reliability, he runs the risk of being punished commercially through an unplanned SPR release that will lower the value of his inventory in the short term. Again, the SPR incentivizes low inventories out of price concern.

Inventory decisions should be left to the marketplace. The marketplace has shown itself to be self-correcting and efficient. SPR decisions to influence price ironically create incentives for refiners and suppliers to hold lower oil inventories, which is bad for the consumer. Lower inventories do not provide a buffer against price shocks caused by sudden increases in demand. To the contrary, low inventories contribute to price spikes.

C. Administrative Concerns

The non-emergency use of the SPR is difficult to administer to assure fairness and adequacy in the distribution scheme. The experience of the 1970's with a government body in charge of gasoline allocation, which resulted in shortages, lines, and allegations of fraud and corruption, shows the dangers inherent in centralized administration of supply and demand.

Finally, once SPR oil is released to the marketplace, it becomes difficult to monitor that the oil is used as intended by the government. It can be traded or sold at a profit, or even exported on the world market, and perhaps the consumer will not benefit.

V. THE OIL MARKET IS NOT SPECULATIVELY DRIVEN, AND A SPR DECISION ON THAT BASIS IS NOT JUSTIFIED

One prevalent theory seeking to justify the release of SPR oil is that the market is driven by speculative forces, instead of commercial ones. The accompanying price charts clearly show a rational market making decisions on the basis of supply and demand information, as known. The SPR release became factored into the price for the short term period it would have a supply impact, and thereafter, the market readjusted to its former price sentiment.

Contributing to the ever-present theories, rumors, and ghost stories of how speculators can drive prices up, are the press releases by OPEC, which minimize the impact of its members' conduct and routinely list "speculation" as the number one cause of high prices. These excuses for a painful consumer environment may make for colorful tales in the news media, but they do not reflect how public markets work today, with hundreds of commercial participants and instantaneous price dissemination. Any "speculative" price would be met with an equally strong "commercial" reaction. An oil company would gladly sell its oil at a speculatively driven "inflated" price. And those sales, in turn, would act to bring the market right into line again.

The reason every major oil company around the world uses our markets not only to manage their risk, but also as a benchmark for transactions in related markets, is that the price activity is consistent with their in-depth understanding of market conditions based on exploration and development projections—industry executives would be more likely than laymen to know whose wells are suffering operating problems or who has a cargo of oil at sea. To the extent that the market begins moving in a direction that is inconsistent with their market intelligence, they will seek to take advantage of it, selling into a market that is reaching too high, thus dampening the price increase and buying into a market that is too low—mitigating the decline. The participation of hundreds of other similar commercial entities—energy producers, wholesalers, retailers—and government agencies with comparable access to information is what ensure the prices will rapidly return to where the industry consensus believes it should be. If the system didn't work, these savvy market players would have found or developed a better one, particularly in this age of instantaneous access to global information.

Speculators do exist and they actually play a valuable, even necessary role—adding liquidity to the market and enabling the commercial traders to get in and out of the market when they need to. By the nature of their role, speculative traders seek to take advantage of price trends, but because they lack the real oil to back up their investment, they cannot control the price, only hitch on for the ride. They create virtually no impact on daily settlement prices, which are the primary benchmark used by the marketplace.

NYMEX has a regulatory responsibility, which is supervised by the Commodity Futures Trading Commission, an independent federal regulatory agency, to monitor market participation and take all necessary steps to protect against price manipulation. The CFTC has consistently found that NYMEX performs its regulatory functions, as required.

Because of the broad national importance of energy prices to the public, the U.S. Department of Energy (“DOE”) has also studied the role NYMEX plays in the pricing of energy. Four years ago, as a result of sharp winter price increases in heating oil in late 1996, the DOE's Office of Policy began a study on the heating oil futures market. The final report, “Heating Oil Futures Markets and Price Volatility” issued last June, concluded that futures markets play a stabilizing role in the determination of heating oil prices, even during a period of sharp price increases. The report also confirmed the extremely broad use of the marketplace by oil refiners (who produce the heating oil, and have a great interest in a “real” unmanipulated price) for hedging their risk. By using the NYMEX market for hedging, the refining community inherently endorses the validity or integrity of NYMEX's pricing mechanism.

Market Oversight

The federal government has long recognized the unique economic benefit futures trading provides for price discovery and managing price risk. In 1974, Congress created the Commodity Futures Trading Commission, giving it authority to regulate commodity futures and related trading in the U.S. A primary function of the CFTC is to ensure the economic utility of futures markets as hedging and price discovery vehicles—encouraging competitiveness, efficiency, and market and trade practice integrity and fairness. The CFTC reviews the terms and conditions of proposed contracts, and oversees registration of firms and individuals who either handle customer funds or give trading advice. It conducts and monitors rule enforcement at U.S. futures exchanges. The CFTC also reports publicly the speculative/commercial ratio of participants in the market.

Under the regulatory framework, NYMEX is both regulated and self-regulating. To fulfill its self-regulatory duties, NYMEX has people and systems in place to ensure that, despite the fundamental forces in operation at a given time, artificial factors or manipulation cannot drive the prices of futures contracts. Our market surveillance and financial surveillance systems ensure orderly markets, including the recent period of price changes in the heating oil market. *Specific self-regulatory functions relevant to this hearing include:*

1. Speculative position limits

Speculative position limits, or a limit on the number of contracts any one participant can hold in a single month or aggregated over all months, are an important facet of market oversight. The limits protect the market from the potential influence of large participants or concentration of positions. Speculative position limits for the crude oil contract are 1000 contracts (1 contract is 1,000 barrels of crude oil) in the spot, or nearby contract month, and an overall limit of 20,000 contracts in all months. NYMEX does permit hedge exemptions to the total number of positions an individual firm or group acting collectively can assume in any one month or all

months combined to accommodate legitimate risk management needs of large commercial firms. There are four strict rules governing the exemptions: first, there must be sufficient liquidity in the market; second, the firm must document its cash market hedging needs; third, the firm must be appropriately capitalized and financially solvent; and fourth, the firm must have the experience to handle the size of the position. These measures serve to avoid domination by any one hedging entity, and assure that each commercial firm has the financial status to perform on its contract obligations. Large positions, defined as those entities holding 300 or more crude oil contracts, are reported to the CFTC and NYMEX daily.

2. Surveillance of Market Fundamentals

Market surveillance also monitors the supply and demand fundamentals in the underlying cash market. This is to ensure that NYMEX reflects cash market price movements, that the futures market converges with the cash market at contract expiration, that there are no price distortions and no market manipulation. Market surveillance staff meets weekly to assess market conditions. The surveillance staff includes members of the compliance, operations, and research departments, and—when necessary—senior administrators.

After analyzing events and developments over the past several months, including the most recent price moves, NYMEX surveillance staff have concluded that the crude oil market price movements were based on a number of fundamental market factors. It is NYMEX's belief that the crude oil futures market performed in a rational manner, that price increases experienced were due to a number of widely identified fundamental market factors including tightened supply and increased demand. Markets were closely monitored and contract liquidation has proceeded smoothly. The NYMEX system worked according to design, providing a viable price discovery and risk management forum—the functions which it is required under federal law to perform.

Once again, on behalf of NYMEX, I wish to thank you for the opportunity to discuss the SPR, and will be happy to answer any questions you may have.

Mr. BARTON. Thank you, Mr. Wolkoff. We will now will hear from Mr. John Surma, who is with the Marathon Ashland Petroleum Company, and they are one of the winning bidders of SPR oil. We recognize you for 5 minutes.

STATEMENT OF JOHN P. SURMA

Mr. SURMA. Thank you very much. As you indicated, I am with Marathon Ashland Petroleum, which I will refer to as MAP. We are the Nation's fifth largest refiner and marketer. We operate seven refineries with a combined crude oil capacity of 935,000 barrels per day. Most of our territory is in the midwest and southeast. We appreciate the chance to present our company's perspective. We were a winning bidder of 3.9 million barrels on the first round of release.

First, let me speak to the supply and demand picture. With respect to the manufacture of heating oil, we believe the efficiency of the free market system is best capable of shifting resources to meet apparent demands. On or about Labor Day, our company began to manufacture maximum distillates in our refining system. In September, MAP set a company record for distillate production of 300,000 barrels per day. Additionally, we are operating at or near maximum levels. All of this is occurring without any influence of the release of crude from the SPR or any other force other than normal market forces.

Our company supports the creation and maintenance of a strategic reserve of crude oil to ensure adequate energy supply in times of emergency. In fact, as a significant purchaser and refiner of crude oil, MAP would look to the SPR in times of emergency to supply refineries and meet the energy and transportation fuel demands of our customers.

The SPR, in our view, represents a critical controllable source of oil in the event of a significant sustained world oil supply disruption. MAP supports the drawdown of SPR crude in the event of a national emergency. We do not believe the current case fits that definition. Based on our experience with the current release, we are concerned about the process by which the government has offered SPR volumes for sale or exchange as well as the ability of the SPR to execute deliveries upon completion of the contracts. We believe these concerns should be addressed and specific procedures defined so that both the DOE and the Nation's refiners are prepared in the event of a true supply emergency.

Let me comment on several specifics. With respect to prequalifications or offer guarantees, we find that purchasing crude oil from the SPR is a serious and complex business transaction, and we strongly support a prequalification procedure for the inclusion of an offer guarantee in all future SPR solicitations similar to that which was included in the most recent October 16 solicitation package.

The package receipt from the DOE for the initial solicitation, dated September 25, 2000, required that an irrevocable standby letter of credit be established in favor of DOE and then be provided to the contracting officer within 5 business days of receipt of award. We complied with that requirement. Three of the successful bidders were granted additional time to comply, even though there was no such provision for extension in the solicitation package. We believe that the solicitation rule should be applied consistently for all bidders, and special rights and exceptions should be avoided. Only then will participants in the auction process be comfortable that they understand the rules and ensure a more efficient bid process in an orderly clearing of the market.

Of the 30 million barrels of SPR crude that was initially awarded, 24.9 million barrels was West Hackberry crude oil. Most of that crude must be shipped to Sun's Midland, Texas terminal for movement to the refiners by pipeline, vessel or barge. We understand that Sun may not be able to handle all of the SPR crude nominated to it in the month of November. As a result, some of the SPR crude oil will likely not be delivered until December.

The uncertainty of SPR deliveries makes it difficult for our country to complete our November crude purchase program, which must be finalized no later than October 25. We suggest that for any future release, that DOE work closely with the connecting terminals to determine what the capacity limitations are and tailor the solicitation volumes appropriately. As the solicitations currently stand, custody transfer for West Hackberry crude takes place at the Sun terminal receiving tanks. In order to maximize volumes through Sun's terminals, MAP suggests that this measurement procedure be modified.

We believe DOE should work with Sun to designate a given number of tanks strictly for DOE deliveries such that custody transfer occurs as Sun delivers out of their tanks to the connecting pipeline, vessel or barge. By making this simple change which is common practice in the industry, shipments from DOE's facilities can be maximized and crude oil can reach its ultimate destination in a more rateable and predictable manner. We believe these recent

events provide further evidence of the need for a comprehensive national energy policy, which recognizes the need for strengthening the downstream infrastructure of the domestic petroleum industry.

That policy should consider the threat to supply that the recently proposed low sulfur diesel rule represents and should also recognize the need to improve the flexibility of the Nation's petroleum refining pipeline and logistics infrastructure.

In closing, we recommend that changes be made to the commercial and logistical program elements which have been problematic in the process such that all market participants, and the general public, will have a greater assurance that the SPR will be able to fulfill its mission in times of a true national emergency. We appreciate the opportunity to be here.

[The prepared statement of John P. Surma follows:]

PREPARED STATEMENT OF JOHN P. SURMA, SENIOR VICE PRESIDENT SUPPLY AND TRANSPORTATION, MARATHON ASHLAND PETROLEUM LLC

Good morning. I'm John Surma, Senior Vice President, Supply and Transportation, of Marathon Ashland Petroleum (MAP). We are the nation's fifth largest refiner, operating seven refineries with a combined crude oil capacity of 935,000 barrels per day. We operate 85 terminals in the Midwest and Southeast United States which distribute gasoline, diesel and asphalt, and we market through more than 5,200 retail outlets in 21 states under the Marathon and Speedway brands. We are headquartered in Findlay, Ohio.

Chairman Barton, Members of the Sub Committee, I welcome the opportunity to present my company's experience and perspective on the recent release of crude oil from the Strategic Petroleum Reserve. Our company was the successful bidder on 3.9 million barrels.

I would like to focus my remarks on a number of issues related to the recent SPR bidding process and the planning for and delivery of the crude oil, but first let me speak to the supply/demand picture. With respect to manufacture of heating oil, we believe the efficiency of the free market system is best capable of shifting resources appropriately. On or about Labor Day, MAP began to manufacture maximum distillate in our refineries. In fact, during the month of September, MAP set a company record for distillate production, over 300,000 barrels per day. Additionally, MAP is operating available refining capacity at near maximum levels. All of this is occurring without any influence of the release of crude from the SPR.

Our company supports the creation and maintenance of a strategic reserve of crude oil to ensure adequate energy supply in times of emergency. In fact, as a significant purchaser and refiner of crude oil, MAP would look to the SPR in times of national emergency to supply our refineries and thus meet the energy and transportation fuel demands of our customers. With the majority of our nation's supply of crude oil coming from outside the United States, the SPR represents a critical, controllable source of oil in the event of a significant, sustained world oil supply disruption. MAP supports the drawdown of SPR crude oil in the event of a national emergency. We do not believe that the latest situation fits that definition.

Every day, our company surveys the oil markets seeking to purchase the crude oil supplies necessary to meet the requirements of our refineries. Once the decision was made to offer oil from the SPR, we were compelled, for competitive reasons, to bid for this crude as we do for other crudes marketed for sale. As the successful bidder for 3.9 million barrels, we in turn will not purchase that amount from other sources. A similar scenario would likely apply to the entire 30 million barrel SPR drawdown. One could infer that an incremental 30 million barrels of crude oil will simply be diverted to the world market. In turn, the 570 million barrels currently in the SPR will be diminished by 30 million barrels until it is replaced sometime next year. The ability of the SPR to mitigate a world supply disruption will therefore be diminished by this amount during the coming year. I would liken this situation to a family spending a part of its nest egg for a luxury item, and not having those resources available should a necessity arise in the future.

Based on our experience with the current SPR release, we are concerned about the process by which the government offers SPR volumes for sale or exchange, as well as the ability of the SPR to execute deliveries upon the completion of contracts. We believe these concerns should be addressed and specific procedures defined so

that both the DOE and the nation's refiners are prepared in the event of a true supply emergency.

Let me comment on several of these issues:

Pre-qualification of Bidders or "offer guarantees"

Purchasing crude oil from the SPR is a complex business transaction involving assessing the current value of the crude oil to the refinery relative to alternatives, handling the logistics to move the crude oil, procuring the replacement crude oil nine to twelve months in the future, hedging the risk in the futures market and posting an irrevocable standby letter of credit. The inclusion of unqualified bidders in this process has been disruptive to the successful, legitimate bidders like MAP. MAP is concerned that these and, perhaps, other bids submitted by companies or individuals who were not bonafide bidders and who submitted unrealistic bids, might have influenced DOE's decision with regard to our original bids which were not accepted in full.

Simply put, the inclusion of unqualified bidders in such an auction process results in a disorderly market and a potentially inefficient result. In the event of a true supply emergency, it would be in the best interests of the DOE, consumers and refiners to avoid market inefficiencies and unnecessary and time-consuming delays resulting from unqualified bidders being involved in the process. MAP strongly supports a pre-qualification procedure or the inclusion of an "offer guarantee" in all future SPR solicitations, similar to that included in the October 17, 2000 solicitation package.

Strict adherence to procedures

The solicitation package received from the DOE dated September 25, 2000, required that an irrevocable standby letter of credit be established in favor of the U.S. Department of Energy and be provided to the contracting officer within five business days of receipt of awards. MAP complied with this requirement. Three of the successful bidders were unable to provide the letter of credit on the due date and DOE granted additional time for these bidders to comply, even though there is no provision for such an extension in the solicitation package. MAP believes that the solicitation rules should be applied consistently for all bidders, and special rights and exceptions should be avoided. Only then will participants be comfortable that they understand the rules, which helps ensure a more efficient bid process.

Terminal logistics limitations

Of the 30 million barrels of SPR crude that was awarded, 24.9 million barrels is West Hackberry crude oil. Most of this crude oil must be shipped to Sun's Nederland, Texas terminal for movement to refiners by pipeline, vessel or barge. We understand that Sun will not be able to handle all of the SPR crude nominated to it in the month of November. As a result, some of the SPR crude oil will likely not be delivered until December. The uncertainty of SPR deliveries makes it difficult for MAP to complete our November crude purchases program with other suppliers that must be finalized no later than October 25. We would suggest for any future release that DOE work closely with connecting terminals to determine what capacity limitations are, and tailor the solicitation volumes accordingly.

DOE measurement requirements

As the Solicitations currently read, custody transfer for West Hackberry crude oil takes place at the Sun terminal receiving tanks. Quantity measurements are based upon Sun's opening and closing tank gauges. No commingling of batches is allowed by DOE. Crude is pumped from Sun's tank to the delivery pipeline, vessel or barge. The next DOE delivery to Sun's tank can take place only after a particular batch has cleared the tank.

In order to maximize volumes through Sun's terminal, MAP suggests this measurement procedure be modified. DOE should work with Sun to designate a given number of tanks strictly for DOE deliveries. Rather than custody transfer occurring as the crude is delivered into Sun's tanks, it should occur as Sun delivers out of their tanks to the connecting pipeline, vessel or barge. By making this change, which is common practice throughout the industry, and allowing for commingling of any West Hackberry batches, shipments from DOE's facility can be maximized and crude oil can reach its ultimate destination in a more ratable and predictable manner. This same concept should be adopted at other DOE facilities if applicable.

We believe these recent events provide further evidence of the need for a comprehensive national energy policy which recognizes, among other matters, the need for strengthening the downstream infrastructure of the domestic petroleum industry. That policy should consider the threat to supply that the recently proposed

“low-sulfur diesel rule” represents and should also recognize the need to improve the flexibility of the nation’s petroleum pipeline and logistics infrastructure.

In closing, we urge the DOE to make every effort to comply with the delivery terms and conditions in the solicitation. Further, we recommend that changes be made to the commercial and logistical program elements that have been problematic in the current process, such that all market participants, and the general public, will have a greater assurance that the SPR will indeed be able to fulfill its mission in times of true national emergency.

Again, I appreciate this opportunity to appear before this Sub Committee, and I look forward to answering any questions you or other members of the Sub Committee may have.

Mr. BARTON. We appreciate you being here. Now we go to Mr. John Manzoni, president of the Eastern United States for British Petroleum.

STATEMENT OF JOHN MANZONI

Mr. MANZONI. Thank you. My name is John Manzoni. I am the Regional President for the Eastern States for BP. I am pleased to be here this morning at the request of the subcommittee to review with you BP’s participation in the recent SPR bidding process. BP is one of the largest energy companies in the world. We explore for, produce, refine, and we market petroleum and other energy products, including solar applications, all around the world.

First of all, I would like to take a few moments to explain how and why we made the decision to bid on the SPR crude oil. Let me be clear that the basis for our decision was purely a commercial opportunity. It is useful to explain how we supply our refineries in order to understand how we approach opportunities in the market and how we approached the SPR.

The first point is that the refiners are supplied by a series of contracts, and those contracts are for various terms or lengths. It is the traders’ job to make sure that the refiners are well supplied with crude oil, and the traders take into consideration several factors. For example, the logistics of getting the oil into the refining, the assay or genetic makeup of the crude oil, whether sweet or sour. And depending on these physical factors, as well as other market factors, the traders will bid a particular price for crude oil where they believe that they can be profitable. This is a complex process, and all of the factors that I have mentioned, the logistics, the assay and the price are interrelated. As a company, we are continuously in the market looking to service our refinery assets to keep them supplied with crude oil into the future, and of course to make a trading profit. In other words, the market is dynamic and it is continuous.

So let us talk about the specific crude oil BP bid on for the SPR. First of all, it was a sweet crude oil and that crude happens to be the best economically available crude to service our refineries. Second, it had easy access to our logistic system. Given these factors, our traders, like others in the market, put a value on the crude and created an exchange ratio because the SPR transaction was an exchange and not an outright purchase. Because of the structure of the market, we were able to offer a commercially attractive ratio, which will deliver more oil into the SPR at the end of the period and at the same time, we were trying to determine how we could derive value on a trading basis, given our view of the forward structure of the price curve.

With these considerations, our traders chose to make a bid on the SPR crude. This transaction worked for us because, as I said, the crude matched with our refinery requirements, and it was close to our logistical system. It was, therefore, the most economically attractive crude to run in our refineries. The terms of the contract were exactly as per the solicitation process. And in the first round of bidding, BP was awarded 2 million barrels of oil.

Then the SPR retendered the second round. Between the first and second rounds, we were able to establish alternative logistics to allow us to move the crude in a different way between the refineries, which allowed us to bid for the 4 million barrels the second time and that amount we were subsequently awarded. This brought our total SPR award to 6 million barrels. We expect to lift all of that oil in November, and furthermore, we expect to process it through our refinery network starting about that time.

As I explained, we carefully consider the supply, the logistic, and the production capabilities of our network when we make crude selection decisions. The entire process is managed using economic and investment decision criteria which are based on sound business practice.

In closing, let me also address the status of BP's operations in the United States. All of our refiners are currently running at maximum available capacity. We are maximizing distillate production and our inventories are at or above normal levels. We have no planned shutdowns for our refinery system for the remainder of this year although, of course, unplanned shutdowns and outages can always occur. Finally we continue to believe that the market mechanism provides the most efficient distribution and allocation of resources in the best interests of our consumers. Thank you for your time. I will be happy to take questions.

[The prepared statement of John Manzoni follows:]

PREPARED STATEMENT OF JOHN MANZONI, BP REGIONAL PRESIDENT, EASTERN UNITED STATES

Good morning Mr. Chairman and Members of the Subcommittee, I am John Manzoni, Regional President of BP for the Eastern United States. I am pleased to be here at the request of the Subcommittee to review with you BP's participation in the recent SPR bidding process.

BP is one of the largest energy companies in the world. We explore for, produce, refine and market petroleum and other energy products, including solar applications, around the world. We are in the markets everyday, constantly seeking to balance our supply and demand obligations, while earning a reasonable return for our shareholders.

First, I would like to take a few moments to explain how and why we made the decision to bid on SPR crude oil. Let me be clear, the basis for this decision was a commercial opportunity for BP.

It is useful to explain how we supply our refineries in order to understand how we approach opportunities in the market, and thus how we approached the SPR. The first point is that our refineries are supplied via a series of contracts for oil of various lengths. It is the traders' job to make sure that the refineries are well supplied with crude oil. As they do their business, there are several considerations they must take into account. For example, the logistics of getting the oil in to the refinery—the transportation cost; the assay, or "genetic" make-up of the crude—whether it is sweet or sour. Depending on these physical factors and other market factors, the traders will bid a particular price for crude oil where they believe they can be profitable. This is a complex process and all the factors are inter-related. We are continuously in the market looking to service our refinery assets, keep them well supplied and to make a profit. In other words, the market is dynamic and continuous.

So, let's talk about the specific crude oil BP bid on from the SPR. First of all, it was sweet crude, and happened to be the best economically available crude to meet our refinery needs; second, it had easy access to our logistical system. Given these factors, our traders, like others in the market, put a value on the oil and created an exchange ratio, because the SPR transaction was not an outright purchase, it was a swap. Because of the current structure of the market, we were able to offer a commercially attractive ratio which will deliver more oil into the SPR at the end of the period. We were trying to determine how we could derive value on a trading basis given our view of the forward price of crude oil. With these considerations our traders chose to make a bid on the SPR oil. This transaction worked for us because the supply was close to our logistical system and it was the most economically attractive crude oil to run in our refineries.

Now allow me to address the terms and structure of BP's bid. The terms of our contract were exactly as per the SPR solicitation. In the first round of bidding BP was awarded 2.0 million barrels of oil.

Then the SPR re-tendered a second round. Between the first and second rounds, we established a logistical alternative to move crude which allowed us to bid for a further 4.0 million barrels, an amount which we were subsequently awarded. This brought our total SPR award to 6.0 million barrels of crude oil. We expect to lift all of the oil in November and process it through our refinery network around that time.

As I have explained, we carefully consider the supply, logistic and production capabilities of our network when making crude selection decisions. The entire process is managed using economic and investment decision criteria that are consistent with sound business practices.

Let me also briefly address the status of BP's refinery operations in the US. All of our refineries are currently running at maximum available capacity. As is usual for this time of year, we are maximizing distillate production and our inventories are at normal levels. We have no planned shutdowns in our refinery system this year; however, unplanned outages can always happen. We continue to believe the market provides the most efficient distribution and allocation of supply in the best interest of consumers.

Thank you very much for your time. I would be pleased to take questions.

Mr. BARTON. Thank you. We will now hear from John Boles, president of Equiva Trading in Houston, Texas. We recognize you for 5 minutes.

STATEMENT OF JOHN BOLES

Mr. BOLES. Thank you, Mr. Chairman. By way of background, Equiva Trading Company is owned by Equilon Enterprises and Motiva Enterprises. Each has a 50 percent interest. Equilon, in turn, is a joint venture owned 56 percent by Shell and 44 percent by Texaco. Motiva's ownership is 35 percent Shell and 32.5 percent each by Texaco and Saudi Refining Company. We are in the business of product supply and trading, crude oil supply and trading, marine charting and support and other related activities.

As you indicated, we are headquartered in Houston with smaller trading offices in Burbank, California and Calgary, Canada. We were not consulted on the September 22 decision to release oil from the Strategic Petroleum Reserve. However, once that decision was made and the oil was released, this created an opportunity for us to participate in the process.

Equiva Trading was the successful bidder on 2.5 million barrels of the release. We learned of the opportunity through the SPR press release on their Web site, and through direct DOE contacts, and submitted a bid in the required format. The process was consistent with other commercial bidding transactions, and was open and fair. We have read in the Wall Street Journal and seen television reports about bidders who were awarded significant volumes of oil without evidence of their financial ability to perform. It is our

opinion that the integrity of the bidding process is enhanced when regular DOE procedures are followed and letters of credit are part of the process. Nevertheless, we were pleased that Equiva was successful in its bid, and I can assure the committee that we will fully comply with all provisions of our contract each and all of which are reasonable and commercial.

We do not have an opinion on the extent to which the SPR release had an impact on supplies of crude and home heating oil. Our parent companies, however, are making efforts to ensure that adequate supplies of home heating oil reach the northeast in a timely fashion, and we have participated in the establishment of the government's home heating oil reserve in New England. Representatives of Motiva and Equiva Trading notified Secretary Richardson that we will not, in the near term, export home heating oil given current market conditions.

Thank you.

[The prepared statement of John Boles follows:]

PREPARED STATEMENT OF JOHN BOLES, PRESIDENT, EQUIVA TRADING COMPANY

Mr. Chairman, my name is John Boles and I am President of Equiva Trading Company, which is owned by Equilon Enterprises and Motiva Enterprises each of which have a 50% interest. Equilon, in turn, is a joint venture owned 56% by Shell and 44% by Texaco. Motiva's ownership is 35% Shell, and 32.5% each by Texaco and Saudi Refining Company. On behalf of Equilon and Motiva, we are in the business of products supply and trading, crude oil supply and trading, marine chartering and support, and other related activities. We are headquartered in Houston, with smaller trading offices in Burbank, California, and Calgary, Canada.

Mr. Chairman, Equiva Trading was not consulted on the September 22 decision to release 30 million barrels of oil from the Strategic Petroleum Reserve. However, once the decision was made and the release was announced, this created an opportunity for us to participate in the process.

The public record will demonstrate that Equiva Trading was the successful bidder on 2.5 million barrels of the release. Like other potential bidders, we learned of the opportunity through the SPR press release on their website and through direct DOE contacts and submitted a bid in the required format. In our view, the process was consistent with other commercial bidding transactions, was open, and was fair.

We have read in the Wall Street Journal and seen television reports about bidders who were awarded significant volumes of oil without evidence of their financial ability to perform. It is our opinion that the integrity of the bidding process is enhanced when regular DOE procedures are followed and letters of credit are part of the process. Nevertheless, we are pleased that Equiva was successful in its bid, and I can assure the Committee that we will comply fully with all provisions of our contract, each and all of which are reasonable and commercial.

We do not have an opinion on the extent to which the SPR release had an impact on supplies of crude and home heating oil. I can, however, state that our parent companies, Equilon and Motiva, are making efforts to assure that adequate supplies of home heating oil reach the Northeast in a timely fashion and have participated in the establishment of the government's home heating oil reserve in New England. Representatives of Motiva and Equiva Trading notified Secretary Richardson that we will not, in the near term, export home heating oil given current market conditions.

Mr. BARTON. Thank you.

The Chair is going to recognize himself for the first 5 minute round.

First, we invited all of the successful bidders to testify, even those that ultimately dropped out. We made a decision not to try to go through the subpoena process to get witnesses from the Secretary on down, simply because we believe in the tradition of the committee, that we do not use subpoenas except in the most ex-

treme case, and we didn't consider this hearing to necessitate subpoenas.

My first question to the bidders: Was there a minimum price calculation that DOE put on the oil? I have heard that there was a \$30 base case valuation on the oil; is that true or not true? For the letter of credit, they had to put some value on the letter of credit. If you have 2 million barrels, that letter of credit had to be valued at some price. Was that the same price in each case; and if so, did DOE stipulate the price for the letter of credit?

Mr. SURMA. I believe in the most recent solicitation document, there was a price specified. It was \$34 and something.

Mr. BARTON. But I am really more interested in the first go-around than the second.

Mr. SURMA. I am afraid I am not as familiar with the first solicitation.

Mr. BARTON. So when you had to put the letter of credit up, what was that based on, Mr. Manzoni?

Mr. MANZONI. I am afraid that I am not familiar with the specifics of the particular trades. We do hundreds of trades.

Mr. BARTON. I understand that.

Mr. MANZONI. Nothing has been indicated to me that there is anything unusual with the letters of credit that are required.

Mr. BARTON. What is unusual is in the first round, apparently anybody, and I mean anybody, could tender an offer, could tender a bid. If you were successful, then you had so many days to put this letter of credit up. This letter of credit had to be based on some valuation of the oil that you were getting because the government owns it and the government and the DOE witness testified that they were guaranteeing that the taxpayers were not at risk. So somebody in your operations put a valuation on the oil that you were successful in getting without any preconditions, and my question is: Who did that? Did your traders do it? Did DOE say here is what the price is?

Mr. MANZONI. In our case, it would have been somebody in our trading organization. I will be happy to submit that for the record.

Mr. BARTON. If each of you could do that, I would appreciate it.

In terms of repayment, there is a timeframe in which you have to repay in kind. In other words, you don't pay money, you pay back in more barrels of oil. What are your timeframes in the contracts, Mr. Surma?

Mr. SURMA. I believe the contract specifies rateable repayment of a certain slate of crude that we specified in our bids from August through November.

Mr. BARTON. So you have from August to November.

Mr. Manzoni?

Mr. MANZONI. I know that the November timeframe is correct, but I am not sure what time we start; but soon.

Mr. BOLES. The same timeframe.

Mr. BARTON. What happens under the terms of the contract if the market goes up, not down? What is your contract extender clause? Is it good faith or is there actually in the contract an eventuality provision if the market is higher than the futures market indicated it will be next year?

Mr. SURMA. My understanding, Mr. Chairman, is that the effects of what the market changes may be is our responsibility, that our contract with the government is to return the specified amount of crude oil.

Mr. BARTON. So if oil is \$50 a barrel next November, you expect to put in the number of barrels that you got out plus some, even if you have to buy it on the open market?

Mr. SURMA. Yes, sir.

Mr. BARTON. And in order to preclude that, my guess is that you have hedged your position right now so that if the market is different, you are hedged against that?

Mr. SURMA. We manage our market risks extensively and carefully, and we are not unaware of that risk.

Mr. BARTON. But you don't expect to go to DOE and say we guessed wrong, we thought prices were going to be \$24 a barrel but they are \$35 a barrel, give us more time?

Mr. SURMA. Our analysis did not include that as an option.

Mr. MANZONI. I think my answer would be exactly the same. We have a commitment to replace a number of barrels, and of course our trading risks, in the same way as stated by Mr. Surma, are carefully managed on a global basis.

Mr. BOLES. We are managing the same way.

Mr. BARTON. Of course, if the price is higher, you wouldn't be opposed if DOE came and said do you want more time?

Mr. SURMA. That would be a separate new decision to make, based on the conditions of the market at that point. I am reluctant to say we would be in favor.

Mr. BURR. Would the chairman yield?

Mr. BARTON. Sure.

Mr. BURR. Do you hedge your exposure with any contracts that might be futures contracts which buy to eliminate that downside risk?

Mr. SURMA. We are actively involved in a variety of energy trading activities that are related to our risk management, both NYMEX and over-the-counter.

Mr. BURR. That is a common practice within the industry?

Mr. SURMA. It would be common in the industry, yes.

Mr. BARTON. Mr. Wolkoff, you talked about certainty in the market and efficiency of operation and stability. In your opinion, as the representative of the New York Mercantile Exchange, is what DOE has done with the SPR, is that promoting certainty and predictability or is that putting volatility and unpredictability into the market?

Mr. WOLKOFF. It is not promoting stability and predictability unless they were to say that it would not be done in this way again. That would promote stability.

Mr. BARTON. So it has put an element of uncertainty in the trader's mind, and in the oil market, there probably is a decline curve over time. If it doesn't happen again, people will say it probably won't happen again. But when we prebriefed the previous hearing a month ago, the DOE representative said that they reserve the right to do this as often as they wanted to. And this time they did it with no prenotification to the Congress. They may have prenotified IEA representatives, but we don't see that on the

record. So you agree with the chairman that this has just created more uncertainty and unpredictability, which long term is a bad thing for the oil market, not a good thing?

Mr. WOLKOFF. Yes, I agree with you.

Mr. BARTON. Mr. Boucher.

Mr. BOUCHER. I want to thank the witnesses for being here and apologize for the length of time you have had to wait today.

A number of the witnesses have mentioned, and some members of this panel have mentioned, the potential problem of disruption in transportation of petroleum products to the northeast and have suggested that perhaps a waiver of the Jones Act to enable foreign flag carriers to participate in that transport might be helpful. I would like the opinion of the witnesses who are involved in the energy market directly, the three gentlemen on this side of the panel, with regard to whether you are witnessing any current disruptions in transportation to the northeast from other parts of the U.S., that the ability of foreign flag carriers to take part in the market might resolve, and if there are no current disruptions of that nature, are there any potential disruptions of that nature lying ahead?

We are trying to decide whether we should enact legislation that would authorize a Jones Act waiver, perhaps, for a temporary period of time directed toward this purpose, and your advice concerning the need for that would be helpful.

Mr. Boles.

Mr. BOLES. Yes. The pipelines moving out of the Gulf Coast and northeast are essentially full, which means marine transport is the primary outlet, and the market for Jones Act vessels is becoming very tight and difficult to arrange. So in the event in a sudden surge in demand, there could be disruptions in terms of our ability to mobilize the necessary resources to move. So the availability of a waiver would provide flexibility to respond to those kinds of events.

Mr. BOUCHER. Mr. Manzoni, would you comment.

Mr. MANZONI. From BP's perspective, we are not constrained currently in the movement of our oil in this particular instance, and so from our perspective we do have sufficient anchorage to move the required oil into the future.

As to the longer term and as to the generic point, one has to agree that any restrictions on mobility are bound to be more problematic than no restrictions, but I think that in this instance, there are multiple constituencies, and it would need consideration. I am not qualified to comment on the Jones Act at this time.

Mr. BOUCHER. Mr. Surma?

Mr. SURMA. We operate largely in the midwest and southeast and don't typically transport a great amount of product into the northeast. Having said that, we do ship on the same pipelines that Mr. Boles mentioned, and they are limited in times of need to move significant amounts of product. Infrastructure limitations are most often what the problem is. To the extent that Jones Act relief would allow additional marine assets to come into play, that would be the most expedient manner to get additional product into the northeast.

Mr. BOUCHER. So having waiver authority in place, that would be preferable?

Mr. SURMA. Yes, sir.

Mr. BOUCHER. Mr. Wolkoff, my question is a response, if you care to make one, to the claims that some members of the subcommittee made earlier today that perhaps, coincident with this drawdown of oil from the SPR, there should be some restriction placed on the ability of that—of U.S. companies taking that oil, to export that oil to other countries. You, I know, are quite an advocate of unrestricted markets and predictability, and I wonder if you have any comment on what those kinds of export restrictions might do to the unrestricted market, which I know that you value?

Mr. WOLKOFF. NYMEX and I, as its representative would certainly be in favor of unrestricted exporting ability as well as importing ability. It is a world market, and I think to disrupt that would be to disrupt the entire supply and distribution network. As I understand the Strategic Petroleum Reserve, however, its use is intended to be applied during a period of defined and declared national emergency, so there is a disruption in supply.

Given such a disruption, it would seem to me to be a fair-minded exception to my general philosophy of free and open markets, that because there is a supply disruption and because there is a national emergency, the lack of an export restriction would be, in my view, somewhat inconsistent. I think it is a matter open to many opinions, but that is in the context of a national emergency.

I think it is fairly clear from events in this particular release that the kind of emergency, actual physical shortages, shutdowns in supply and the like, was not the case. So in this particular release of SPR, I think entering into an export restriction would have probably just made a bad decision worse.

Mr. BOUCHER. Thank you.

Mr. BARTON. Mr. Burr is recognized for 5 minutes.

Mr. BURR. Thank you, Mr. Chairman.

I think my good friend, Mr. Boucher, misunderstood where some of us were going with our questions of DOE as it related to an export restriction. There were two points that were trying to be made, at least by this member. One, that the possibility exists for companies to reallocate those planned imports or to choose to move the reserves that they brought out of SPR. They have the free flow to respond to the marketplace, in essence. Given that they made a decision not to put market restrictions on, I think you are right, Mr. Wolkoff, that there was not an emergency, yet every statement from the Department of Energy publicly and from the administration was that this was not an action from the release of SPR to address the price spike.

There is an inconsistency here. If there is a shortage and that shortage is to the degree that there is an emergency, then it would have made perfect sense for the administration and for the Department of Energy to put restrictions on the distribution of this SPR product, and I do believe the financial markets would have gone along with that.

Let me go to the futures market.

What we do today or say today does not have an effect on the price tomorrow. If it does, it is not the same magnitude as it does 6 months from now; is that an accurate statement?

Mr. WOLKOFF. If it does, I have clearly said the wrong thing.

Mr. BURR. Noted.

Secretary Summers and Chairman Greenspan were accurate in their memorandum to the President, weren't they?

Mr. WOLKOFF. I have never read the memorandum to the President. I have read excerpts to the memorandum to the President. And in all honesty, I am not familiar with the circumstances of that memo having been written, whether it was intended as a preliminary memo or a final judgment. So I can comment on it, but really only from a secondhand knowledge of what they said in it.

Mr. BURR. Given the lack of a thorough debate within the Department of Energy as it related to the Secretary's memorandum to the President, the fact that it was a memorandum to the President, it wasn't a memorandum to the Secretary of Energy, it wasn't a memorandum to the area of DOE that deals with SPR release, it gives one the impression that this was an imminent decision to be made by the White House and the Secretary of the Treasury thought it important enough to send the memo directly to the President, President of the United States.

Chairman Greenspan felt it important enough for it to be part of the memorandum to the President, and I think, although we could dissect, and I think did with the Department of Energy, each piece that Secretary Summers addressed, the overall theme was the concern that they had on the precedent that would be set in the marketplace. The government at will, without clear explanation releasing part of the reserve into the marketplace of petroleum products, and their expression was long term, this is a very, very bad precedent to set. Do you agree?

Mr. WOLKOFF. Yes, I heard that recited by one of the witnesses today. I actually thought it was a very well articulated point, and I do agree with it.

Mr. BARTON. Would the gentleman yield?

Mr. BURR. I would be happy to yield.

Mr. BARTON. We asked the Treasury Department to testify at this hearing, and after various negotiations, they ended up not testifying, although as late as yesterday afternoon they were testifying. But the three officials that helped prepare that memo, 2 of the 3 are no longer at the Treasury Department, and the third has apparently become seriously ill very quickly, and we don't know whether that is a legitimate illness or a political illness, but we were not able to get the Treasury officials here or you could go into more detail.

Mr. BURR. I think that the Secretary's position and the chairman's position were both stated very clearly, unlike the reason why we are releasing SPR.

Let me turn to the three gentlemen that were successful in their bids. If in September, I think that was the timeframe on the first contract, September—

Mr. BARTON. This is your last question this round.

Mr. BURR. If the bid requirements stated not 100 percent but 110 percent of the value in the letter of credit, would that have changed your bid price or your willingness to bid?

Mr. SURMA. I don't know that it would have affected our willingness to bid. We viewed this as a commercial source of supply. The letter of credit cost, there is a cost element to it, it was an economic

element in the valuation. To the extent that would have been a greater amount, that would have had an effect. I can't say how much, but some element.

To the best of my knowledge, I think we, for at least economic valuation purposes, used relatively current market prices to decide how much that would be.

Mr. MANZONI. We have no difference with that answer.

Mr. BURR. So the 10 percent would have affected potentially the replacement bid?

Mr. SURMA. Yes, sir.

Mr. BURR. Okay.

Mr. BARTON. We will now go to Mr. Shimkus.

Mr. SHIMKUS. Thank you, Mr. Chairman.

Of the three industry individuals, Marathon, BP and Equiva, how long would you stay in business if you were purchasing crude oil high and selling it low? Could you sustain your market and capital and stay in business?

Mr. SURMA. That is not an element of our strategic plan.

Mr. SHIMKUS. And I am having nods across, that is not really a way to stay in business.

Since the Federal Government's role in the strategic petroleum reserve, taxpayers have foot the bill for over \$420 million because of purchasing high and selling low. In my opening comments, when I was defending the honor and integrity of the chairman, which I like to do, I think that is one of the things that he has always been harping on, we don't know when to buy and we don't know when to sell. We are a government, we are not involved in really the business industry as we like to think that we are sometimes. That is why a lot of us are queasy about our being involved in the market. Because we are very inefficient. We are inefficient in our ability to do our job here as designed by the founding fathers; and especially involving ourselves in the market, we don't add any value when we get involved in the market.

In the first contract offer, was there not a stipulation to keep the crude oil in country?

Mr. SURMA. I am not aware if there was. We are not involved in any kind of exportation. It wouldn't have been a relevant issue for us to focus on.

Mr. MANZONI. I am not actually aware of any specific terms in that particular contract.

Mr. BOLES. The same answer.

Mr. SHIMKUS. If you could just recheck, because I think in our initial hearings, we asked that of the DOE and I was under the impression that there was.

Mr. BARTON. They told me that there was no restriction on the oil used. The only restriction was that you actually had to take the oil from the reserve. You couldn't leave it in the reserve and buy or sell it. You had to take it out of the reserve. That is what I was told before the bid.

Mr. SHIMKUS. Mr. Surma, your market area is—could you explain it again?

Mr. SURMA. Midwest and into the southeast to some degree. Mostly in the midwest.

Mr. SHIMKUS. So as far as your purchase of the SPR, do you have marketing capabilities for home heating oil in the northeast?

Mr. SURMA. No, sir.

Mr. SHIMKUS. So your purchase would not have affected any of the home heating oil debate in New England?

Mr. SURMA. We do make some fuel that would be in the home heating category, but it would be on the periphery of the northeast market.

Mr. SHIMKUS. How many barrels did you purchase?

Mr. SURMA. 3.9 million.

Mr. SHIMKUS. Mr. Boles, I want to ask, I have been very interested in the northeast heating oil reserve and you say that you are involved with that. Explain that to us. The question that I asked in the last hearing, how come the administration before we went to the SPR, why didn't they release—they had at least 1.5 million barrels of heating oil of reserves on hand, and why didn't they release those instead of going through the auction of the SPR?

Mr. BOLES. Our only involvement is as a supplier. We provided a million barrels of supply into the reserve, and are also providing 500,000 barrels of storage. It is a commercial relationship.

Mr. SHIMKUS. Where is that storage at?

Mr. BOLES. I believe it is in New Haven.

Mr. SHIMKUS. Mr. Chairman, thank you.

Mr. BARTON. Mr. Burr is recognized for 5 minutes.

Mr. BURR. I won't take that long, Mr. Chairman.

Mr. Wolkoff, did the Department of Energy consult with the marketplace in any way that you are aware of that the impact a sale of SPR might have?

Mr. WOLKOFF. NYMEX was not part of a consultative effort. I cannot speak for any efforts that took place with any other companies.

Mr. BURR. But you are not aware of any?

Mr. WOLKOFF. I have not heard of any other discussions, but that is not to say that they didn't happen.

Mr. BURR. The price of a barrel of crude was what on the day that DOE announced a plan to sell SPR, do you know?

Mr. WOLKOFF. It was around 34 and went down to 33. It had been as high as 37 several days prior to that, but because of stories of impending releases and the like, the market—and perhaps for many other reasons, one is hard-pressed to ever know why the market does what the market does.

Mr. BURR. The price is what today?

Mr. WOLKOFF. The price of a barrel of NYMEX light sweet crude was as high as \$37 several days before the SPR release. The previous day before the announcement it was \$34 and went down to \$33, \$32.50. In that area.

Mr. BURR. Where is it today?

Mr. WOLKOFF. Today it is about \$33. It peaked again last week with the Mideast hostilities, but it has gradually come back. As of yesterday it was about \$33.

Mr. BARTON. If the gentleman would yield, this was as of 11 this morning. It opened at \$32.80 for light crude deliverable in December, and it was at \$32.70 per barrel. Heating oil opened at 96 cents for December delivery and had gone up to 96.7 cents a gallon .

Mr. BURR. I thank the chairman for that accurate information. My point, and I think you have answered it, is that since this announcement, the price has fluctuated significantly, over \$4 a barrel, based upon nothing that the Federal Government did, but on the perceptions of the world marketplace?

Mr. WOLKOFF. I am not sure that I understood that characterization. I think that the price went lower prior to the actual announcement of SPR; and since the announcement, the price in the short term went down \$1 to \$2. It went back up apparently in response to the Mideast events, and has proceeded to come back down again.

Mr. BURR. I define that as fluctuation. It went down, it went back up and back down.

Mr. WOLKOFF. Price movement without knowing the cause.

Mr. BURR. Next week it could go back up. Clearly the release of SPR has had no effect on the stabilization of the pricing. The marketplace has a greater effect on the stability of the price?

Mr. WOLKOFF. I can't totally agree with that. I think it has had some near term effect on the price. There are other elements out there that on any given day can make price fluctuations happen. But when you look over the course of several weeks and you compare the price at the time of the SPR release, or just prior to the SPR release with the price, and the price I have most recently is October 17—

Mr. BURR. If Venezuela took their 2.3 million barrels, which is their current output off the marketplace, would the price go up or down?

Mr. WOLKOFF. It would depend on what anybody else in the market did. If that were the only action that day and there is generally not one taking that kind of supply off the market, it would raise the price.

Mr. BURR. If they were doing that for good, what effect would it have on the price?

Mr. WOLKOFF. Without any other substantive events, it would increase the price.

Mr. BURR. I don't want to hold you over after this vote, so I yield back the balance of my time.

Mr. BARTON. The Chair recognizes himself for a few questions. Before the gentleman leaves, the Chair would ask unanimous consent that all members not present have the requisite number of days to put their statements in the record. The staffs have the ability to prepare materials to be put in the official record. Is there an objection? Hearing no objection, so ordered.

To my three bidders, the first question I have, what would have happened had the SPR release not have occurred? Was there a shortage of oil that you would have to curtail refinery operations, or in Mr. Boles case, bidding for crude had they not released the oil?

Mr. SURMA. In our case, we were operating at or near capacity, and the incidence of the release or not really would not have affected our refining operations at all.

Mr. BARTON. Mr. Manzoni.

Mr. MANZONI. I have exactly the same answer.

Mr. BARTON. Mr. Boles.

Mr. BOLES. We were not short on supply, no.

Mr. BARTON. So what you basically did was just substitute this oil for other oil that was on the market because it was a better deal economically; is that correct?

Mr. BOLES. Yes.

Mr. BARTON. Mr. Martin, we have not asked you a question yet. You talked in more global terms in your opening statement, so I am assuming that you are following the world oil market. Have you been made aware of some of the discussions more of a political nature than an economic nature, that there has begun to surface some talk of another oil embargo against the United States because of what has happened in the Middle East in the last month?

Mr. MARTIN. I am not aware of that.

Mr. BARTON. You are not aware of that? Do you think the release of this oil in the SPR would give more credibility or less credibility to those in the OPEC cartel that, for political purposes, would want to politicize the use of their production capacity again like they did in the 1970's and 1980's?

Mr. MARTIN. It gives us less credibility.

Mr. BARTON. My last question, and then I will go do Mr. Markey who got here literally in the nick of time. The underlying trend in this whole debate is that we do not have enough refinery capacity in the United States because our refineries are operating at capacity and we haven't built a new refinery in the last 10 to 15 years. Do you gentlemen that did the bidding on the oil believe that we should add additional refinery capacity in the United States.

Mr. Manzoni, you are smiling.

Mr. MANZONI. I shouldn't have been.

Mr. BARTON. You are allowed to smile. It is not against the rules of the subcommittee to smile.

Mr. MANZONI. I feel only qualified frankly to answer from our own perspective, and our own perspective with regard to refinery investments is that this is a part of our business which is central, which is strategic, which has to be invested in. These investments are very big. They are very long term. The fact is that the returns on those investments have not been stellar over the history, and that, obviously, impacts economic and commercial decisions about the level of investment in them. So those are the considerations that we take into account as a company when we consider refining stock and refining investments.

Mr. BARTON. I am not asking from an economic standpoint whether it makes sense from your company's perspective to add additional refinery capacity. I am asking from an economic standpoint in the United States to assure supply of refined products, do we need to add to the refinery base in the United States kind of generically or as opposed to whether it makes sense for your company to put money up? That is my question.

Mr. MANZONI. I mean, if I may, without trying to be evasive, if I may go to a comment that has been made several times here, I think the supply and demand of both product, crude and everything else in the United States is quite a holistic problem. The holistic energy policy, which deals with the investment patents to the logistics and the refining and the marketing aspects, that is abso-

lutely required, in our view, and we certainly would be interested in participating in a constructive and bipartisan conversation.

Mr. BARTON. Mr. Surma.

Mr. SURMA. I would generally support that. Most public demand forecasts suggests that any reasonable growth in transportation fuel and heating fueling, those kinds of products is likely to outstrip refining capacity at some point, which leads then to greater product imports, which leads to more dependence on international trade, that to some degree, energy sufficiency and independence on the refining side is something we, the country, has had for a long time and we think is worth defending, and that means additional capacity.

Mr. BARTON. Mr. Boles, do you have a comment on that?

Mr. BOLES. I would agree with those comments.

Mr. BARTON. Mr. Martin, again, strategically do you think it is important that we add additional refinery capacity in the United States as opposed to importing more refined product?

Mr. MARTIN. I think it basically should be an economic question, but strategically yes, I think so. I think we face a challenge in energy infrastructure generally in the United States. That is why I was happy that you are having these hearings on gas infrastructure, refinery infrastructure and so forth. We can't depend on overseas forever, because they have demands themselves, and that demand is growing very, very rapidly. That is again why I want to say about the SPR, this was really a silly reason to use a very valuable national security asset. We are going to need to use that SPR I think within 5 years for a serious concern, whether it is an embargo, whether it is a disruption, whether it is a war. And what we are finding all the time our reliance is going up, but so is everybody else's in the oil market.

Mr. BARTON. Have you voted?

Mr. MARKEY. No.

Mr. BARTON. We will recognize you for as long as possible until we both have to go vote. The gentleman from Massachusetts.

Mr. MARKEY. I thank the gentleman very much.

I know that I was gratuitously insulted in absentia by Admiral Watkins. And I thought I would return the compliment. And it is only to say this, I know that Admiral Watkins has a very strong, ideologically based position in terms of whether we should deploy the strategic petroleum reserve. In fact, on August 2, 1990 when Saddam Hussein invaded Kuwait, the oil prices in the world skyrocketed from \$16 a barrel to \$36 a barrel. We had an emergency hearing in this committee a couple of weeks later, and we asked Admiral Watkins, who was Secretary of Energy to come and testify. He said he was on vacation and he couldn't make it. He really didn't think it was important for him to come back to testify because he did not believe that the strategic petroleum reserves should be deployed in that circumstance, which, of course, was war.

Now, they never did deploy it until actually a couple days before we began bombing January 15, 1991. But for August, September, October, November, December, January, the price of oil stayed up there. Now, the end of 1991 a little mini recession started to hit America, the beginning of 1992. That was the oil recession, \$36 barrel oil ripping its way through our economy. Now ironically,

George Bush Sr. won the war but lost the election because he didn't deal with the oil component of it. He started to get blamed for the economy, which a lot of people say he just did not get.

What we are trying to say here, notwithstanding Admiral Watkins' lack of ability to understand his own personal history in creating the recession of 1991 and early 1992, is that we were going to try to avoid it this time by using the very same weapon that he was not willing to use then. We used it because OPEC ministers meeting together would be a per se violation of antitrust law in the United States.

Mr. BARTON. There are less than 2 minutes in the vote on the floor.

Mr. MARKEY. Thank you, Mr. Chairman.

We have no power to deal with that per se violation. The only real weapon we have is to flood the market with as much oil as we can to limit their ability to artificially inflate prices that ultimately would rip through the western economy. I still think that Admiral Watkins doesn't get it. He didn't get it once. I think it would be a mistake for us to allow him to dictate policies that would have the American—

Mr. BARTON. It would be helpful if you could encourage your Secretary of Energy—the current Secretary of Energy to come to these hearings so we can hear from the current Secretary of Energy. Then we could hear the official position from the people that made the decisions. He was invited and said he had to be in Canada today. The current Secretary is apparently in Canada today and the Under Secretary is in the Senate today. I am not sure where the Deputy Secretary is, but he is not here, so that the Acting Assistant Secretary, who is a civil servant, a true soldier, that is, who the Clinton/Gore Administration put forward for this hearing.

Mr. MARKEY. If I may, again, return to the subject so history records this correctly. The military Secretary of Energy in 1990 did not want to come to our hearing, when we did have a crisis and they never did do anything. This civilian Secretary of Energy, Hispanic Secretary I might add, did do something about it and we are already seeing the benefits in our economy with the lowering of the prices by \$6 to \$8 a barrel. That is the difference. Our secretary really doesn't have to show up because he already did the job. And thank God Secretary Watkins showed up 10 years late, still not understanding the mess that he helped to create.

Mr. BARTON. We want to thank the gentleman from Massachusetts for his editorial comments. We want to thank this panel for your attendance. There may be other questions in writing for the record. We would hope that you would provide them expeditiously. This hearing is adjourned.

[Whereupon, at 2:08 p.m., the subcommittee was adjourned.]

[Additional material submitted for the record follows:]

PREPARED STATEMENT OF DAVID W. WILCOX, ASSISTANT SECRETARY FOR ECONOMIC POLICY, DEPARTMENT OF TREASURY

Mr. Chairman, Mr. Boucher, Members of the Committee, this testimony addresses the President's decision to swap 30 million barrels of oil out of the Strategic Petroleum Reserve for replacement next fall.

Let me begin by noting that the overall prospects for the U.S. economy are very good today, despite the current conditions in world petroleum markets. One clear

confirmation of this fact comes from the latest consensus economic forecast released last week by the Blue Chip panel of some 50 economists at major businesses, financial institutions, and economic research organizations. The consensus view is that U.S. economic growth will remain strong in the near term, and inflation will remain moderate. The Blue Chip forecasters expect real GDP growth to average 3.3 percent during the second half of this year, and 3.4 percent (fourth quarter to fourth quarter) during 2001. They forecast CPI inflation at 2.9 percent for the second half of 2000, slowing to 2.6 percent next year.

In addition, the Blue Chip panel released last week their semi-annual update of the outlook for the next 10 years. Once again, the picture looks strong. The consensus forecast of the Blue Chip economists is that real GDP will grow by at an average annual rate of 3.3 percent from 2002 through 2011. This is up from 3.1 percent in the ten-year forecast compiled last March and 2.7 percent in the October 1999 forecast. Inflation is expected to remain tame, with the CPI rising at an average annual rate of only 2.6 percent over the ten-year horizon.

Turning specifically to the issue of the swap from the Strategic Petroleum Reserve, the Administration believes that this policy has a sound economic rationale.

Use of the SPR in response to low inventories of crude oil was a policy option that had been on the table most of the year. But in the several weeks before the swap announcement, the world oil market became considerably more unsettled. The price of oil surged by more than \$3 a barrel to its highest level since the Gulf War. We saw anecdotal reports of anticipatory purchasing that seemed to be generated by the expectation of a further price rise.

Most important, domestic stocks of both crude oil and refined products were at an unusually low level. There was growing concern that we might not have sufficient inventories of home heating oil to ensure a smooth supply through the winter. In the Northeast, in particular, stocks of distillates are down by about half from last year's levels. All told, the tightness of the petroleum markets left very little room to absorb any further shocks, raising the risk of very unfavorable developments in the months ahead.

The deterioration of market conditions led the President to take a prudent, precautionary step to reduce the risk of shortages of home heating oil this winter. The President ordered that about 5—percent of the SPR be made available for the swap, leaving the other 95—percent in reserve for possible future use. We anticipated that this measured action would have several favorable effects:

- First, and most directly, the swap would increase the supply of crude oil and boost oil inventories.
- Second, the swap would increase the supply of home heating oil this winter. Although domestic refineries were operating around 96 percent of capacity in July and August, we expected that capacity utilization would decline in the early fall, as it usually does, at the conclusion of the period of peak demand for gasoline. In fact, that decline in utilization has now occurred—and with utilization around 91 percent, refineries have the capacity to refine oil from the SPR.
- Third, the swap could reassure markets that there would be no disruption in the supply of oil, thereby adding confidence to what could potentially have been a difficult situation. By rebuilding inventories, we can reduce the likelihood of shortages and spikes in the price of heating oil and other refined products this winter.
- Fourth, by using SPR reserves for an exchange rather than an outright sale, we will have a larger Strategic Petroleum Reserve next fall than we have today, leaving us with an enhanced energy security in the long run.

While it is too early to observe any increments to inventory levels, the behavior of the oil market since the swap announcement suggests that we are on the right course:

- The markets reacted to reports that an exchange was imminent. The 1-month futures price of West Texas Intermediate dropped more than \$3 per barrel on rumors of the pending announcement, and then by more than \$1 per barrel on the announcement of the President's decision. Moreover, the price continued to head downward over the following six calendar days, for a cumulative decline over that period of more than \$2 per barrel. Overall, from the day before to six days after the President's action, the one-month futures price of WTI dropped by about \$7 per barrel.
- Importantly, the one-month futures price of heating oil also declined during this same period, taking very much the same profile from day to day as crude oil prices. While the objective of the policy was to address potential issues of supply disruptions and shortages, we cannot lose sight of the fact that in markets, shortages—and potential shortages—are reflected as higher prices. Likewise, al-

leviation of shortages—and reductions in the risk of shortages—are reflected as reductions in prices.

- Since that time, a portion of the oil price decline has been reversed. This partial unwinding appears to be due primarily to additional concerns about instability raised by recent world events such as the turmoil in the Middle East, a hurricane threatening production in the Gulf of Mexico, an early cold snap in the Northeast, and Venezuelan oil workers going on strike.
- It is noteworthy that, notwithstanding those world events, crude oil prices remain several dollars a barrel below where they were before the SPR swap announcements. In addition, the 1-month futures price of home heating oil is also well below its level a month ago, despite substantial volatility arising from these market forces. These readings suggest that the SPR swap is viewed by market participants as having reduced the pressure in petroleum markets and the risk of shortages this winter.

In summary, we believe that the swap has given market participants, and U.S. citizens generally, a measure of confidence they would not otherwise have had that the Federal government is ready and willing to move aggressively to address issues of supply disruptions. In a market as tight and unsettled as the world oil market is today, every additional measure of confidence is extremely valuable. Mr. Chairman, we believe that the U.S. economy is in better shape today because the President undertook a SPR swap.

Thank you.