AMERICA AT RISK

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Testimony before

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Good afternoon, I am Denise Bode, Vice Chairman of the Oklahoma Corporation Commission. The Oklahoma Corporation Commission is a constitutional body composed of three state-wide elected officials responsible for the prudent management of our natural resources, as well as regulating gasoline, electric, natural gas, telecommunications, water utilities, and transportation. Previously, I was President of the Independent Petroleum Association of America during its application for trade relief under section 232 of the Trade Expansion Act. I greatly appreciate the opportunity to share my concerns regarding the efficiency and effectiveness of the Executive Branch's response to rising oil prices.

Mr. President, America is at risk because of our heavy dependence on foreign oil. Unfortunately, the policies of this Administration have caused our dependence on foreign oil to grow twice as fast as during the previous twenty years since the Arab oil embargo.

To understand how and why America is at risk, first understand that there is not a "free market" in the traditional sense when it comes to oil. There never has been. My friend, Dan Yergin's Pulitzer Prize-winning book on oil, The Prize, articulates convincing rationale that oil markets have always been manipulated, first by the Standard Oil Trust, then by our government through pro-rationing and price controls, and finally by OPEC through producing nation quotas. While the development of commodity contracts through NYMEX complicated the ability of oil producing nations to manage the market, the education of those playing that market about the importance of OPEC has now been complete and they are back in the drivers seat. And we have watched oil producing countries manipulate their oil inventories for politics as well as their own economic gain. Our reliance on foreign oil has gone from 34% during the 1974 Arab oil embargo, to 44% in 1992, to close to 60% today.

The problem is that each time the OPEC cartel manipulates oil supply to create shortages or to flood the market, it causes price shocks making the domestic oil production industry a less stable business, which in turn drives away investment, terminates qualified employees, and destroys valuable infrastructure, both exploration and refining. And it forces more of US. production, 40% of which is marginally economic, to be plugged and lost forever. It is so serious now, that even with the latest OPEC price increases, domestic producers are not drilling new domestic oil wells. Out of approximately 800 rigs drilling, less than a third of those are drilling for oil. And these price shocks impact consumers as well by making it impossible to make a family budget without knowing whether gasoline will cost $0.70 or $2.00 a gallon.

In 1993, at the beginning of this Administration, OPEC cartel production and thus imports to the U.S. were up. Oil prices in the US. fell below $13 a barrel and imports had risen to 44 percent. Domestic refineries had dropped to around 190 and domestic refining capacity was still close to meeting U.S. consumption. The Independent Petroleum Association of America petitioned in March of 1994 under section 232 of the Trade Expansion Act for an investigation into increasing oil imports and action by the President. Since the Eisenhower Administration, this trade act has been used to affect American energy policy relations with the world. While the Administration was "contemplating" the petition, a bipartisan group of members of Congress presented him an energy plan that would maintain a strong domestic production and refining option. That plan included:

- A tax credit to preserve marginal production
- A tax credit to encourage new drilling
- Elimination of tax penalties and updating of tax rules on geological and geophysical cost, percentage depletion, and enhanced oil recovery
- Open up access to production in frontier areas on federal lands, like ANWR
- Provide for federal royalty reductions for marginal production and production in frontier areas like the deep Gulf of Mexico
- Look at environmental laws that were duplicative and overreaching
- Resolve federal royalty collection problems that limit production of natural gas

No action was taken on their plan. A year later a presidential finding of a national security threat was finally issued with no new actions proposed. But the presidential finding did warn us of what we would be facing without action. Specifically it said, **"the United States and its allies may find themselves constrained from pursuing either unilateral or multilateral foreign policy actions for fear of provoking producer countries into actions that could result in the manipulation of oil prices and increased prices for consumer countries."**

During that time, domestic oil production dropped by over 500,000 barrels a day, imports accelerated, and 75,000 Americans lost their jobs.

Congress took the initiative to enact one item in their plan, a royalty holiday on Gulf of Mexico deep water drilling. This new production stopped the decline in domestic production by 1997, clearly demonstrating our ability to spur domestic production.

The most significant energy policy initiated by the Clinton Administration during that time was a 4.3-cent increase in the gasoline tax.

The OPEC cartel clearly understood that U.S. energy policy was based on instant gratification, seeking low gasoline prices from foreign sources and ignoring future consequences with a foreign cartel in charge of our transportation fuel and our prices. So in 1997, members of OPEC acted to consolidate their control of the American market by increasing production and reducing world oil prices to historic low prices. Of course, there were other economic factors they hadn't adequately predicted that drove the price down even beyond their control. But the US. took no action and another 30,000 Americans lost their jobs. Domestic oil production went from holding steady to a 5.4% decline, an incredible drop of another 600,000 barrels a day. Today we have only 153 refineries down from 198 in 1990. Even when OPEC cut production to raise oil to $30 a barrel, domestic production has not been increased. Members of Congress clamored for another investigation of the threat to our national security of oil imports. The second Presidential finding in this administration was released at the end of March, again finding an increasing national security threat.

Twenty-eight states have taken the initiative with incentive programs for production. Since 1998, eleven states have enacted 25 new incentives to save domestic production, including Oklahoma, which acted in special session to enact a reduction in the gross production tax when prices fall. I proposed a fuel tax holiday for consumers, similar to the one passed from the gross production tax for producers, to protect consumers from OPEC shock.

The Clinton Administration says they were "caught napping" when fuel prices jumped. I would suggest otherwise. With two Presidential findings of national security risk in hand, they "knowingly" put American consumers at risk for these high prices with the foreign policy of looking to the OPEC cartel for more oil imports and gasoline instead of acting to stabilize domestic production and refining capacity. Of course, not all of the OPEC cartel are our friends. Since 1997, Iraq has been our fastest growing supplier of oil, now accounting for about 700,000 barrels per day. Current imports are approximately 11 million barrels per day.

Regrettably, after Administration policies left America highly vulnerable to OPEC supply reductions, its requirements for new fuel additives actually aggravated the problem and contributed to today's price spikes in the Midwest. Speaking as a regulator of gasoline and the oil and gas industry in Oklahoma, I am disturbed by the notion that this Administration would sanction the implementation of new stringent standards on additives to gasoline on June 1 at the very beginning of the peak season for gasoline use. A responsible regulatory approach would have been to implement new requirements on a schedule that is less likely to cause severe disruption to consumers. Development of contingency plans also should be done when there is potential for significant disruption. These are not extraordinary practices. They have been our practice at the Oklahoma Corporation Commission when implementing new regulatory requirements on this industry.

The Administration knew that the production increases they lauded in March were not sufficient to bring down prices going into the driving season. But listening to the President's comments the day he was lauding his work with OPEC, he set up the oil industry as his scapegoat when the economic reality of too little production was felt in the summer. Now some in the Administration claim there is not economic reason for such increases. I disagree. Our current situation is a foreseeable result of an industry that is stripped of its infrastructure and stretched thin by government intervention being ordered to get new products to users in quantities that hadn't been predicted. Experts at the Congressional Research Service and the Energy Information Administration in recently issued reports agree.

Oklahoma is in the same PADD II distribution region as the upper Midwest. We saw the price begin to increase as demand outstripped product. In fact, demand in PADD II exceeds refining capacity in our region this year by close to 25 percent thanks to the loss of refinery infrastructure. So we all depend on pipelines from the Gulf. And with domestic production down to approximately 40 percent, we depend on imports getting to the ports, refined and put into those pipelines. Obviously, with such a tight situation any disruption anywhere is going to impact the market. There were several pipeline disruptions in the spring as suppliers were trying to build up inventory. Demand for gasoline is much higher than industry analysts had forecasted. And now with environmental rules already requiring as many as 38 different kinds of gasoline, it is predictable that adding the major changes required to make reformulated gasolines, particularly ethanol which has to be blended at the rack, to go only to specific U.S. markets would greatly contribute to disruption of the marketplace. In Oklahoma, spikes in price began in June when this changeover to reformulated gasoline began.

As these complicated infrastructure issues are resolved, gasoline prices will continue to fall. Hopefully we have learned lessons in regulatory policy from this government caused disruption.

That is the smaller, more temporary matter. The much more important, fundamental issue is whether we as a nation have learned the importance to our national security and economy of maximizing domestic refining and production options. If we have not learned that fundamental lesson this episode will be replayed in the future with even more costly effect.

We have new evidence of the ability in America to reduce our vulnerability by producing oil here at home. A study just released by the Energy Information Agency of the Department of Energy predicts that if production were allowed from the Alaska National Wildlife Refuge then there was a 95 percent probability that at least 5.7 billion barrels of oil could be recovered. At peak production this could increase domestic production by 1.9 million barrels per day (bpd). Since the Alaska pipeline could hold another 1 million-bpd, because of the decline in other Alaskan production, that increase could dramatically increase our energy security. At present we produce around 5.8 million-bpd and import around 10.4 million-bpd.

In addition, the environmental threat of increasing foreign oil imports is now coming to light. According to the Senate Energy Committee, at 65 percent dependence more than 30 giant supertankers, each with 500,000 barrels of crude, would be docking at US. ports every day. That is more than 10,000 ships passing American coastlines unloading oil in American harbors. The environmental risk posed by tanker traffic is exponentially higher than American production, according to the U.S. Coast Guard. In fact, American production is subject to the strictest environmental requirements in the world. Elimination of domestic production opportunities is an exercise in pseudo-environmentalism.

I agree with former National Security Advisor Perle who believes America needs a viable domestic production option to protect American consumers and deal with any adverse actions towards them by the OPEC cartel. The list provided by the Bipartisan group of members of Congress to the President in March of 1994 is a good starting point. Just think where we would be if we had only encouraged the preservation of all those marginal wells and opened up ANWR for production back in 1994 when the threat to American consumers was clearly articulated in that first Presidential fmding. There is tremendous promise for oil and, particularly, natural gas in America.

Winston Churchill once said, “Men occasionally stumble over the truth, but most of them pick themselves up and hurry off as if nothing had happened.” Control of transportation fuel by the OPEC cartel and the dire condition of the domestic production and refining infrastructure are compelling truths that Americans cannot afford to hurry by one more time.