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Carl Levin, Chairman
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STATEMENT OF SENATOR CARL LEVIN
Permanent Subcommittee on Investigations
Hearing On
Gas Prices: How Are They Really Set?
May 2, 2001

Good morning. Today the Permanent Subcommittee on Investigations will hold its second of two hearings on the reasons for dramatic fluctuations and recent increases and in the price of gasoline.

On Monday of this week the Subcommittee released the report of the Majority Staff following their 10-month investigation.

One of the basic conclusions of the report deals with the effects of increased concentration in the oil industry on the wholesale supply market.

Due to a series of refinery closures and mergers within the oil industry, the wholesale supply market is now more concentrated than ever. According to information provided by the Department of Energy's Energy Information Administration, the wholesale supply market is moderately to highly concentrated in a total of 37 states. By another accepted measure, 28 states are considered tight oligopolies.

In general, more competition means lower prices for consumers and lack of competition leads to higher prices. The oil industry is no exception to those general rules.

In areas of high concentration where a few refiners control most of the retail sales by keeping supplies tight, refiners can raise the price of gasoline without great fear of competition. One way to maintain a tight supply is keeping only a minimal amount of gasoline in inventory. One effect of doing that is that any supply disruption will cause a shortage of gasoline because there is no reserve capacity to bring to market. This invariably leads to price increases, and, because gasoline is such an essential commodity in our lives today, most Americans have no choice but to pay more and more when prices rise.

Keeping supplies tight and inventories low in highly concentrated areas, makes it possible for companies to spike prices without great fear of competition. Since all the companies maintain minimal inventories, no company need fear a competitor will gain market share by keeping their prices low, because they would quickly run out of gas. Mr. James Carter, Regional Director for ExxonMobil for the United States testified to that on Tuesday. He said:

"If our price is extraordinarily low, we are going to run out before the next amount of gasoline gets here. "

So, the few companies in these areas raise and lower prices together and in the same price relationship to each other, a practice called parallel pricing.

One of the key findings in the staff report is that in a number of highly concentrated markets oil companies are not just passive actors who respond to whatever the supply and demand situation is at a given moment, but rather they are active players seeking to shape and structure the market in such a way so as to make the refining business more profitable for them.

The investigation found a number of documents – which we discussed Tuesday – indicating that oil companies seek to tighten supply in highly concentrated markets to increase prices.

While the oil company executives who testified on Tuesday said either that their companies didn't adopt the options set forth in their memo to limit supply or didn't have any knowledge of the activities discussed in another memo, or that actions described in a

memo were against current corporate policy, the evidence presented in the Majority Staff Report demonstrated times when refiners acted to limit supply to raise prices.

Most of the oil companies that testified on Tuesday do not believe we need additional refineries in the United States. These companies believe that the lack of any new refineries has not been a cause of any of the recent price spikes. What this means is that the problem is not how to build more refineries, but how to expand or better use the refining, storage, and other resources we already have in this country.

Although the price of crude and government regulatory actions obviously have a large effect upon wholesale and retail prices in this country the staff investigation looked at actions taken by the oil companies that were within their control, and actions downstream from the crude oil production process.

Today we will hear from a number of distinguished public officials and economists about this subject.

First, we will hear testimony from Senator Ron Wyden. Senator Wyden has been working on the issue of gasoline prices and industry concentration for a number of years.

Following Senator Wyden, we will hear from a panel of Attorneys General. Attorney General Jennifer Granholm is here today from my home state of Michigan. Attorney General Granholm has been very active on a number of consumer issues, including gasoline pricing in Michigan. She successfully forced gasoline stations that gouged the public after the tragic events of September 11 of last year to return their ill-gotten gains.

Attorney General Richard Blumenthal from Connecticut is on our panel today, too. Attorney General Blumenthal has also been active in gasoline pricing issues. Over a number of years he has aggressively advocated for a competitive gasoline marketplace on behalf of Connecticut motorists.

I am also pleased that Mr. Thomas Greene, Assistant Attorney General from California, will be here to represent the California Attorney General's views. As our Majority Staff Report shows, the effects of high concentration and vertical integration in the refining and marketing industries are acutely seen and felt by consumers in the State of California. A few years ago the California Attorney General issued a report on gasoline pricing in that state. That report addressed many of the issues we have been looking at. So we look forward to your testimony here today, Mr. Greene.

On today's second panel we will hear from four economists. All four of these panelists have studied one aspect or another of the petroleum industry, and we look forward to hearing from them.