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ENERGY PROGRAM

13

OIL IMPORT POLICY, CERTAIN EXCISE TAXES AND ENERGY TRUST FUND PROPOSALS

PREPARED FOR THE

COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES

BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

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INTRODUCTION

This pamphlet is the thirteenth in a series prepared for use by the Committee on Ways and Means during its consideration of the tax proposals in the Administration's energy program.

This pamphlet deals with issues affecting imports, including quotas, duties, an import auction licensing system, and oil swaps. Secondly, the pamphlet discusses two miscellaneous excise tax topics: (1) the excise tax on rerefined lubricating oil and (2) the excise tax on radial tires. Finally, the pamphlet discusses the possibility of an energy conservation and conversion trust fund.

Unlike the issues discussed in previous pamphlets, there are no Administration proposals concerning the areas discussed here. These issues were considered by the committee in the 94th Congress, however, and this pamphlet focuses on those deliberations.

Each topic is divided into several subparts. A background section outlines certain facts concerning the energy situation in the area under consideration. A section on present law follows. Next there is a discussion of the legislative proposals considered in the 94th Congress. Alternative proposals offered by the members of the Ways and Means Committee are set forth in the next section. Finally, there is a discussion of possible areas for committee consideration.

In the 94th Congress, the major bill considered in connection with energy tax proposals was H.R. 6860. This bill was reported by the Ways and Means Committee and was amended on the House floor. Markup sessions on H.R. 6860 were held by the Finance Committee in July 1975, and tentative decisions were made in many areas, but the bill was not reported at that time. Many of the provisions approved by the Finance Committee were added to H.R. 10612, the Tax Reform Act of 1976, as title XX, but all of the energy provisions were deleted in conference. In August 1976, the Finance Committee reported the provisions of title XX (as passed previously by the Senate in H.R. 10612) as an amended version of H.R. 6860. This bill was never taken up on the Senate floor and the provisions expired with the adjournment of the 94th Congress.

Unless otherwise indicated, the provisions discussed below with respect to action in the 94th Congress reflect H.R. 6860 as approved by the Ways and Means Committee. Also, unless otherwise specifically indicated, references to the Finance Committee bill refer to title XX of the Tax Reform Bill (as passed the Senate) and the Finance Committee reported version of H.R. 6860. Floor amendments are specifically noted.

I. OIL IMPORT POLICY

A. Background

Petroleum is the most significant single energy source in the United States. In 1976, it accounted for 47 percent of U.S. energy consumption and for more than 95 percent of energy consumed in transportation. The total amount of oil consumed in the United States doubled between 1950 and 1970; except for a slight decline at the bottom of the 1974 recession, U.S. oil consumption has continued to rise.

Domestic oil production has declined steadily since 1970 when production peaked at approximately 4.1 billion barrels.[1] By 1976, domestic production declined to approximately 3.6 billion barrels.[2]

The inevitable result of rapidly increasing oil consumption and declining domestic production has been a significant growth in oil imports. Until 1965, the United States was self-sufficient in oil because its spare (unused) productive capacity for crude petroleum exceeded its oil imports. However, since 1972, domestic production has proceeded at full capacity and imports have risen steadily. In 1976, oil imports amounted to 7.3 million barrels per day (mbd), or 42 percent of consumption.

Without any change in policies, there is likely to be a significant increase in our dependence on imported oil in future years. The Federal Energy Administration estimates that under current energy policies, oil imports will be 48 percent of consumption in 1980, 50 percent of consumption in 1985, and 58 percent of consumption in 1990. These FEA estimates are consistent with independent private forecasts.

The United States imports oil principally from Venezuela, Arab countries, Canada, Iran, and Indonesia. In 1975, the United States was dependent on Arab suppliers for about 650 million barrels of imports, or about 11 percent of its consumption. (Iran supplied an additional 180 million barrels of imports, or about 3 percent of U.S. consumption.) This dependence on Arab suppliers clearly increased in 1976.

Moreover, many U.S. allies, including Japan, Germany, France, and the United Kingdom, have relied on imports for more than 95 percent of their oil needs in recent years. These countries have relied on Arab suppliers for one-half to three-quarters of their total oil consumption. Except for the United Kingdom, which may become self-sufficient as a result of North Sea oil production, these countries will continue to rely heavily on imports in the future.

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[1] Estimate of production of crude petroleum includes natural gas liquids.
[2] Staff estimate based on data for part of year.

B. Proposals Affecting Import Policy

1. Import quotas

Present law

At present there are no quotas imposed on the importation of petroleum or petroleum products. However, if the Secretary of the Treasury determines that imports of petroleum or petroleum products threaten to impair the national security, the President is authorized to adjust the imports by such measures as quotas or duties.[3]

Administration proposal

The Administration proposal does not contain any provisions regarding the imposition of quotas on the importation of oil.

The Administration does propose to increase the strategic petroleum reserve from its current level of 500 million barrels to 1 billion barrels.

Action in the 94th Congress

The House bill (H.R. 6860) imposed restrictions on the quantity of petroleum and petroleum products which could be imported into the United States. The levels of the quotas were based on estimates of energy need, available resources, and conservation savings resulting from the bill, as well as from voluntary efforts.

Beginning with the establishment of an import licensing system in 1975, a maximum limit would have been placed on the average daily number of barrels of petroleum and petroleum products which could be imported in each calendar year. The maximum average daily number of barrels (in millions) was:

1975	6.0
1976	6.0
1977	6.5
1978	6.0
1979	6.0
1980 and thereafter	6.5

If the President determined that, because of variations in domestic consumption caused by economic factors or the weather, because of delays in increasing domestic production or in achieving oil conservation goals, or because of similar factors (such as needs of the Armed Services), it was in the national interest to modify the quotas, he could vary the quota levels. Under the bill, the President could modify the quota either upward or downward by 1.0 million barrels per day (mbd) for 1975–77, 1.5 mbd for 1978 and 1979, and 2.0 mbd for future years. However, the President was required to reduce import quotas to the extent necessary to reflect fully in reduced imports any savings in U.S. consumption of oil.

The bill also provided limited exceptions and separate allowances in connection with the quota restrictions. For 1975 and the first 2 full calendar years of the restrictions, 1976 and 1977, the quotas were to allow the importation of distillate fuel oil and residual fuel oil in an amount equal to an average of 2 million barrels per day. Of this 2 million barrels per day allowance, distillate fuel oil imports could consti-

[3] Section 232(b) of the Trade Expansion Act of 1962, Public Law 87–794 (as amended).

tute a maximum of 400,000 barrels per day. This separate allowance included only distillate and residual fuels used primarily for heating buildings and generating electricity; oil imported under this allowance could not be used as motor vehicle fuel. The residual and distillate fuel oil imported under this separate allowance were to be counted against the quotas.

Imports of petroleum and petroleum products when imported for use in the production of man-made products (such as nitrogen fertilizer, farm chemicals, paints, plastics, synthetic fibers, synthetic rubber, pharmaceuticals) and similar man-made products manufactured from petrochemical feedstocks were not to be counted against the import quota.

Any oil imported for storage in a strategic reserve provided for by law was also exempt from the quota restrictions. (An exemption from quotas for imports of crude oil, petroleum products and natural gas liquids for a strategic oil reserve has since been enacted as part of the Energy Policy and Conservation Act, P.L. 94–163.)

The bill also required the President to divide the quantitative restrictions among the various types of petroleum and petroleum products where divisions were necessary to avoid serious adverse effects on the economic and health needs of industries and geographical areas.

Except for periods of military attack, war, or the introduction of U.S. armed forces into hostilities, the bill ended the President's authority to impose import restrictions on oil under the national security provisions of the Trade Expansion Act of 1962.

The Senate Finance Committee did not consider this part of H.R. 6860.

Alternative proposals

Mr. Vanik

Quotas would be put in place effective January 1, 1979, with quota levels established by the President based on levels of anticipated demand and the amount of needed conservation. Congress could accept or adjust the quota levels within 60 days.

Mr. Steiger

A quota system would be established for imports of petroleum and petroleum products, with an auction system for selling licenses for the right to import under the quotas. The President would have authority to vary the quotas (within limits). Separate quotas would apply in the first years to distillates and residual fuel oil. Petroleum products used for certain purposes (such as nitrogen fertilizer and farm chemicals) would not be subject to the quotas. Separate auctions would be held for licenses of small, independent refiners and marketers.

Areas for committee consideration

Because the United States depends on imported oil for a large percentage of its oil supply and because only a few countries are the sources of worldwide oil exports, the United States is vulnerable to politically motivated supply disruptions, such as the Arab oil embargo of 1973–74. Unlike the problem of resource depletion, the threat of supply disruptions is potentially an immediate one. Such dependence on oil imports from a few countries places serious constraints on U.S. foreign policies.

Although the strategic petroleum reserve currently being implemented (1 billion barrels) could provide up to one year's protection against import disruption from Arab countries (who supplied 830 million barrels in 1975), reducing imports is the most direct way to reduce vulnerability to an embargo. Policies which reduce domestic demand or increase domestic production will reduce imports, but it may be appropriate to consider policies aimed directly at import reduction.

In setting any oil import policy, the impact of that policy on consumer costs, the environment, conservation, national and regional economic stability, the U.S. balance of payments, energy self-sufficiency or dependence, and international economic and political relations must be evaluated. Some opponents of oil import restrictions have suggested that the United States should adopt an energy policy of importing and stockpiling as much foreign oil as possible in order to preserve domestic resources. This approach assumes continued reliance on petroleum as the major U.S. energy source and indifferent reaction by oil exporting nations. It further assumes that the United States can afford to spend huge sums currently for purchasing and storing foreign oil.

However, if the committee decides that some limitation on U.S. oil imports is desirable, it will have to determine whether quotas, duties, or some combination of both best serve to decrease U.S. demand for foreign oil. Specifically with regard to import quotas, a determination must be made about whether the restrictions promote domestic production and conservation, or whether they would deplete domestic reserves too rapidly, leaving the United States even more dependent on imports in the future.

If quotas are to be imposed, appropriate levels must be determined. In H.R. 6860, quotas were set at 6.0 million barrels per day (mbd) for both 1975 and 1976. However, U.S. imports actually amounted to 6.03 mbd in 1975, and 7.27 mbd in 1976. Even though the bill allowed the President to adjust quotas by 1 million barrels per day above the basic quota levels for those years, that flexibility probably would have been insufficient to fill the U.S. demand for foreign oil in 1976.

2. Import duties

Present law

Under present law, import duties are imposed on all petroleum and petroleum products imported into the United States. These duties vary according to the grade of petroleum or type of product. For example, imported crude oil is currently subject to duties of 5¢ or 10¢ per barrel according to the gravity of the oil. This duty reduces the amount of the import license fees administered by the Federal Energy Administration.

Under the President's national security authority,[4] specific import license fees of 21 cents and 63 cents are presently imposed on each barrel of imported petroleum or petroleum products, respectively. The President has discretion to raise or lower these fees and there are no statutory limits on the amount of the permissible adjustment.

Administration proposal

The Administration proposal does not contain any provisions regarding import duties.

Action in 94th Congress

The House bill replaced the present system of specific duties on imports of petroleum and petroleum products with a system of ad valorem duties. It also limited the President's authority to increase or decrease these duties.

The ad valorem rates of duty applying to imports of petroleum and petroleum products provided in the bill were to be assessed by the U.S. Customs Service under valuation standards set forth in sections 402 and 402a of the Tariff Act of 1930, as appropriate. In general, the value for these purposes is the value of the article at the foreign port of exportation.

The bill imposed a 2-percent ad valorem duty on crude petroleum, and a 5-percent ad valorem duty on certain petroleum products. These rates of duty replaced the specific import duties, fees, etc.

The President could adjust the rates of duty established by the bill whenever he found such adjustments necessary to carry out the purposes of this bill, in the light of overall considerations of the national interest. However, the bill limited the Presidential adjustments, so that no rate of duty could exceed 10 percent ad valorem or $1 a barrel (whichever was greater), nor fall below 2 percent ad valorem.

One further limitation on the President's authority to adjust the rate provided that for 2 years after the date of enactment, the President could make no adjustment which resulted in a rate of duty of more than 5 percent ad valorem on any distillate fuel oil or residual oil imported for use as fuel, other than in the propulsion of motor vehicles.

The President was to proclaim all adjustments to the rate of duties on oil imports. Any adjustment increasing duties was to be set forth in a document and transmitted by the President to both Houses of Congress, on the same day, while they were in session. Adjustments could take effect no sooner than the close of the sixtieth day after the date of delivery of the document containing the adjustment to the Congress.

The bill expressly nullified any Presidential adjustments of imports of petroleum and petroleum products under authority granted him under the Trade Expansion Act of 1962 (sec. 232(b)), effective 60 days after the date of enactment of the bill.

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[4] Section 232(b) of the Trade Expansion Act of 1962, Public Law 87-794 (as amended), provides that if the Secretary of the Treasury determines that imports of an article "threaten to impair the national security," the President may adjust imports of that article. Before 1973, this Executive authority over oil imports was exercised by imposing quotas. In 1973, President Nixon switched from adjustment of oil imports through quotas to adjustment through the imposition of monetary exactions called import license fees. This license fee system, which continues today, was upheld as within the President's authority to adjust imports in *Federal Energy Administration v. Algonquin SNG, Inc.*, 426 U.S. 548 (1976).

An exception to the restrictions on Presidential discretion was made for military or defense emergencies involving actual hostilities. The President would have continued to have the full discretion which he has under present law to adjust imports of petroleum and petroleum products during a period in which the Congress declares war, the United States armed forces are introduced into hostilities pursuant to statutory authorization, a national emergency is created by attack upon the United States, or the United States armed forces are introduced into hostilities under circumstances which require a report by the President under the War Powers Resolution (sec. 4(a)).

The bill also provided that where, under the Trade Expansion Act of 1962 (sec. 232(b)), increases in duties had already been made, these duties were to cease to be effective 60 days after enactment of the bill. The rates of duty provided in the Tariff Schedules of the United States were to be replaced by the rates of duty imposed by the bill. The bill further restricted Presidential discretion with regard to oil imports by barring any adjustments of oil import duties under authority granted the President by the Trade Act of 1974, which generally allows him during the five-year period ending January 3, 1980, to enter into trade agreements with foreign countries providing for mutual modifications in import duties or restrictions. Finally, the President could not grant to petroleum or petroleum products from developing countries the duty-free treatment which the Trade Act of 1974 would have allowed the President to provide under appropriate domestic and foreign development conditions.

These provisions were not acted upon by the Senate Finance Committee.

Alternative proposals

Mr. Vanik

A *deminimis* ad valorem tariff would be established to aid in monitoring the quantity and quality of oil imports.

Areas for committee consideration

If the committee decides to increase import duties on oil it may want to follow the general trend of recent U.S. tariff legislation and adopt ad valorem duties, as the House did in the last Congress, instead of the specific duties imposed by present law. The rates may have to be set higher than they were in H.R. 6860, if the duties are to have any impact on imports. The committee may also want to give the Executive some authority to adjust the duties, for example, if energy conservation and conversion efforts effectively reduce demand for foreign oil, or if the national interest requires it. Different types and qualities of oil may be subjected to different rates or levels of tariffs. The committee will have to determine if certain types of petroleum or petroleum products, for example, residual fuel oil used mainly for residential heating, should have lower duties than other types.

Another alternative would be to review the existing Presidential authority to prescribe import duties and tariffs.

It should be noted that tariffs and quotas both serve much the same purpose. Tariffs at a sufficiently high level have the effect of discouraging imports. Tariffs also increase the cost of oil, thus tending to encourage conservation, or the conversion from oil to some other fuel. Quotas prohibit imports above a certain level. To the extent that the demand for oil exceeds domestic production plus the permitted level of imports, quotas tend to drive up oil prices.

3. Import auction licensing system

Present law

No import auction licensing system has been established under present law. However, present law grants the President broad discretion to establish a Federal petroleum import purchase plan which may entail an auction system for reselling petroleum imports. The Energy Policy and Conservation Act of 1975[5] enables the President to establish a procedure whereby the United States Government acts as the exclusive importer and purchaser of all or any part of the foreign crude oil, residual fuel oil, and refined petroleum products brought into the United States for resale. In exercising this purchase authority, the President is allowed to resell the imports by competitive bid. Any Federal purchase plan must be transmitted to the Congress where it is subject to an either-House veto for 15 calendar days before it can become effective.

Administration proposal

There is no provision for an import auction licensing system in the Administration proposal.

Action in the 94th Congress

The House bill also established an import auction licensing system to be conducted by the Federal Energy Administration for distributing rights to import petroleum and petroleum products. Rights to import petroleum and petroleum products (i.e., import licenses) were to be distributed by sealed bidding in public auctions and the licenses were to be fully transferable in the open market.

The bill also provided a second, separate import auction licensing system for small refiners and independent marketers. However, in order to avoid the speculation possible in a two-level market, the separate import licenses could not be resold except to the Deputy Administrator for Petroleum Import Licensing, under the circumstances and to the extent provided in regulations prescribed by him.

The separate import licenses for small refiners and independent marketers were to be established by setting aside what the Deputy Administrator for Import Licensing determined to be a sufficient portion of the quota to meet their needs to the extent not already covered in the general program. These import licenses ordinarily were to be distributed in the same manner as import licenses distributed in the general program—by sealed bids in public auctions. However, in two specific circumstances, the Deputy Administrator was to sell separate import licenses to small refiners or independent marketers at the average price established at the general public auctions (rather than using the separate auction price for small refiners and independent marketers). These special sales of import licenses were to be permitted if (1) a small refiner or independent marketer established to the Deputy Administrator's satisfaction that, despite reasonable efforts, he had been unable to obtain sufficient licenses to maintain his regular level

[5] Sec. 456, P.L. 94–163 (as amended), amending the Emergency Petroleum Allocation Act of 1973.

of operations, or (2) emergency circumstances (such as loss of oil supplies due to the destruction of or damage to his business facilities) required that he be granted licenses to continue his business.

To participate in the separate import license program, a small refiner's total refinery capacity (including the refinery capacity of any person who controls, is controlled by, or is under common control with the refiner) could not exceed 50,000 barrels per day. To qualify as an independent marketer, a person had to be engaged in the marketing or distribution of refined petroleum products and could not be a refiner nor a person who controls, is controlled by, is under common control with, or is affiliated with a refiner (other than by means of a supply contract).

The bill created an Office of Petroleum Import Licensing within the Federal Energy Administration. An FEA Deputy Administrator was to head the Office and administer the program established by the bill.

The bill also contained a provision stating that refiners in the territories, possessions, and foreign trade zones of the United States were to participate in all appropriate aspects of the program established under the oil import title of the bill on terms no less favorable than those set for domestic refiners. This provision was not to have any operational impact, nor to change in any way the status of these refiners under the United States customs laws. The products of these refiners imported into the United States were still to be subject to both the quotas and duties imposed on all oil imports by the bill.

These provisions were not acted on by the Senate Finance Committee.

Alternative proposals

Mr. Vanik

The Federal Government would become the sole authority permitted to purchase and import foreign oil.

Mr. Rangel

The U.S. Government would act as sole importing agent of all crude oil, petroleum products and natural gas, which would be resold at public auction.

Mr. Steiger

In connection with the establishment of import quotas, an auction system would be created for selling licenses for the right to import under the quotas. Separate auctions would be held for licenses for small independent refiners and marketers.

Areas for committee consideration

If the committee decides to impose oil import quotas, it will probably also wish to consider the issue of an import auction licensing system.

As indicated above, under present law, the President has discretionary rather than mandatory authority to establish an auction licensing system if he exercises his authority, subject to a congressional veto, to become the exclusive purchaser of imported oil.

If quotas are imposed, the committee will probably wish to impose an import auction licensing system (or some similar device) on a mandatory basis. In addition, the committee may wish to prescribe by legislation many of the ground rules under which this system will be required to operate.

The committee will have to decide whether to create a "market" by means of an auction system, or whether to have standards established for a rationing or allocation system. Under any government system, the committee will have to determine whether smaller or less competitive domestic refiners or distributors, certain geographic regions or economic sectors, or others, require special treatment or protection.

If the committee decides to adopt an auction system, instead of the two separate auctions provided under H.R. 6860, a single auction could be held with a separate allocation set aside for emergency circumstances. Small refiners and independent marketers who, despite bona fide bids fail to obtain necessary supplies in the auction, could purchase oil from the separate allocation. To encourage competition in the auction, oil from the emergency allocation could be sold for the average price of successful bids in the auction.

In either a two-auction system, or a one-auction system with a special allocation for small refiners (whichever the committee might adopt), speculation in the resale of licenses might be reduced by prohibiting or limiting the resale of the licenses for small refiners and independent marketers.

Another alternative to H.R. 6860's auction license system would be a license allocation program by States or regions. An auction system, however, entails fewer administrative problems than an allocation system. Also, it better simulates market operations and is less subject to allegations of political favoritism.

Apart from the issue of the import auction licensing system, some have suggested that the United States might be in a better bargaining position, with respect to imported oil, if the U.S. Government were given exclusive authority to purchase imports. As indicated above, the President now has this authority on a discretionary basis. It may be that under certain circumstances the U.S. Government would be in a better bargaining position than individual oil companies *vis a vis* foreign governments which export oil. However, due to the current world shortage of oil, it may be anticipated that foreign governments will continue to have substantial bargaining power in this area for the foreseeable future.

4. Oil swaps

Present law

Under present law, import duties are imposed on all petroleum and petroleum products imported into the United States regardless of the import arrangements involved.

Under present law, domestic United States oil may not be exported except under specified conditions. The President may allow exports of U.S. crude oil or natural gas only if he determines that such exports are in the national interest. In making such determinations, he is specifically required to take into account the need to have uninterrupted or unimpaired—

(1) exchanges in similar quantity for the convenience or increased efficiency of transportation with persons or the government of a foreign state,

(2) temporary exports for the convenience or increased efficiency of transportation across parts of an adjacent foreign state for exports which then reenter the United States, and

(3) the historical trading relations of the United States with Canada and Mexico.

Under the Trans-Alaska Pipeline Act of 1973,[6] domestic crude oil transported by pipeline may be swapped for a similar quantity with persons or the government of an adjacent foreign state for convenience or increased efficiency of transportation, or may be temporarily exported for convenience or increased efficiency of transportation across parts of an adjacent foreign state, only if the oil re-enters the United States. The Presidential determination to allow such exports must be submitted to Congress. If the Congress does not pass a concurrent resolution of disapproval, the exports can occur after 60 calendar days have passed.[7]

Administration proposal

The Administration proposal does not contain any provision regarding oil swaps.

Action in the 94th Congress

In 1976, the Senate adopted a Finance Committee amendment to the Tax Reform Act of 1976 (but which was deleted in conference) to provide duty-free treatment of oil imported from Canada under company-to-company oil swap arrangements made pursuant to agreement between the governments of the United States and Canada. (The Finance Committee reported version of H.R. 6860 also included this provision.) The Senate Finance Committee believed that the provision would help protect refiners in the Northern Tier States who depend on supplies from Canada, which has adopted a policy of reducing its exports to the United States.

Under the Senate provision, the United States tariff schedules were to be modified to exempt oil imported from Canada into the United States from the import duties set forth in Schedule 4, part 10 of such schedules, if the oil was imported as part of an oil swap arrangement. The types of petroleum eligible for such swaps were crude petroleum (including reconstituted crude petroleum) and crude shale oil. The

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[6] P.L. 93–153, as amended.

[7] "The Export Administration Amendments of 1977," H.R. 5840, as agreed to by the conference committee (H. Rept. No. 95–354, *Cong. Rec.*, H4628, 4629 and 4633, May 18, 1977) and passed by the Senate and House would modify existing law. The bill prohibits exports of domestically produced crude oil transported by pipeline for two years after the date of enactment unless the exports qualify under limited statutory exceptions. The first excepion exempts the exchanges permitted under the Trans-Alaska Pipeline Act of 1973 from the prohibition. The second exception permits exports if the President makes and publishes express findings that the exports will not diminish the total quantity or quality of petroleum available to the United States; that the export will affect consumer oil prices positively by decreasing the average of refiners' crude oil acquisition costs, that the export is in the national interest and that it is in accord with the provisions of the Export Administration Act of 1969. The President must submit these findings to the Congress. The export may occur only after the expiration of a 60-day legislative period during which either House may veto the export. The bill requires that any contract for export or sale of oil allowed under these exceptions may be terminated if U.S. petroleum supplies are interrupted or seriously threatened.

quantity of imported Canadian oil exempted from U.S. duties had to be equivalent in amount, kind and quality to the oil which was imported by Canada from United States refiners during the 30-day period preceding the date of entry of the Canadian oil into the United States.

The amount of Canadian oil entering the United States duty-free could not be offset against any merchandise except the oil exported by United States refiners to Canada. In order for the Canadian oil to qualify for duty-free entry, the oil exported by United States refiners under the swaps was required to be either domestic United States oil or oil from foreign sources on which United States refiners had already paid the United States import duties.

Alternative proposals

Mr. Rangel

The President's authority to authorize exchanges of Alaskan oil would be eliminated except for exchanges for Canadian domestically produced oil or gas.

Areas for committee consideration

The committee may wish to consider the extent to which (if any) it wishes to provide for duty-free treatment in the case of oil swaps.

In addition to U.S.-Canadian swaps, oil swaps with Japan may be economically desirable. By January 1978, the Alaskan North Slope crude oil production going to the West Coast of the United States may total 500,000 barrels a day more than West Coast refineries can handle. No adequate, economical means of transporting this excess to the Midwest or Eastern States presently exists. Therefore, intra-company sways of North Slope crude oil for crude oil purchased for Japan have been suggested. The crude oil destined for Japan, generally purchased from Arab countries, could be transported through Eastern and Gulf Coast ports to the East and Midwest. In exchange, North Slope crude oil could be shipped from Alaska or the West Coast to Japan. Both countries would save on transportation costs and the United States might not have to construct costly new pipelines.

II. CERTAIN EXCISE TAX PROVISIONS

A. Repeal of Excise Tax on Rerefined Lubricating Oil

Background

Rerefined lubricating oil is previously used oil which has been recycled or rerefined to remove the various impurities which have accumulated in it during use. Used oil is collected from waste oil from such sources as automotive service stations, maintenance garages, railroad yards, industrial plants, and other places of activity where petroleum lubricating oil either is used or discarded. Industry sources estimate that over 1 billion gallons of used oil is available annually for reprocessing. However, only about 100 million gallons of that total are rerefined; the balance is discarded, generally in an environmentally unsafe manner.

Rerefining experience, and tests conducted by the Bureau of Standards, have established that recycling used oil can make it suitable for a variety of purposes. Moreover, the rerefining process not only conserves lubricating oil, but makes any residue safe for disposal in an environmentally acceptable manner.

Present law

Present law imposes a rather complicated scheme of excise taxes, exemptions from tax and refunds of tax with respect to lubricating oil. These provisions have the net effect of discouraging the use of rerefined lubricating oil, at least when blended with new oil.

In general, a six-cent per gallon manufacturers excise tax is imposed on the domestic sale of lubricating oil. (Cutting oil is not subject to this tax.) Also, a manufacturer of lubricating oil will be liable for the tax if he uses the oil himself rather than selling it (unless the oil is used in manufacturing a product which is subject to a manufacturers excise tax).

Cleaning, renovating, or refining used oil is not considered to be manufacturing, so the sale of recycled or rerefined oil by a refiner is not subject to the excise tax. However, where new lubricating oil is mixed with waste or rerefined oil, this does constitute manufacturing, and the excise tax is imposed on the portion of the mixture which consists of new lubricating oil.

Although present law taxes most sales of lubricating oil, present law also allows a tax refund or credit where lubricating oil is used for any purpose other than lubricating a highway motor vehicle. No refund is available where the oil, including rerefined oil, was exempt from tax in the first place. However, present law also denies the exemption where part of the oil was exempt from tax. As a result, when new oil and rerefined oil are blended, a tax is imposed on the new oil portion of the blend, but no refund or tax credit is available. Thus, the tax laws provide a disincentive to the use of new or recycled oil.

In nontax areas, Congress has recently acted to encourage the use of recycled oil. Under section 383 of the Energy Policy and Conservation Act (Public Law 94–163), various Federal agencies are instructed to encourage the recycling of used oil, and to promote the use of the oil so processed or rerefined. The purpose of this mandate is to reduce the consumption of new oil by using recycled oil where appropriate, and to reduce environmental hazards and wasteful practices associated with the disposition of used oil. Recycled oil is to be tested to determine the uses for which it is substantially equivalent in performance to new oil; existing Federal rules pertaining to the labeling of recycled oil are to be changed so that recycled oil which is substantially equivalent to new oil will not be labeled to connote that it is less than equivalent to new oil for a particular purpose. In addition, the Act instructs Federal officials to revise procurement practices to encourage the procurement of recycled oil for military and nonmilitary uses whenever such recycled oil is available at prices competitive with new oil procured for the same use.

Administration proposal

The Administration proposal does not contain any provisions regarding the excise tax on rerefined lubricating oil.

Action in the 94th Congress

Both the House-passed version of H.R. 6860 and the Finance Committee's energy provisions would have removed the tax disincentive for the use of waste or rerefined oil, under certain circumstances, by exempting new oil from the tax when it was mixed with waste or rerefined oil.

Under these provisions, all of the new oil in a mixture was to be free from the tax if the blend contained 55 percent or less new oil. If the mixture contained more than 55 percent new oil, the rerefiner still was to be exempt from tax, but only with regard to the portion of the tax on so much of the new oil as did not exceed 55 percent of the mixture. However, in order to insure that this provision operated in a manner which required the use of a significant amount of waste or rerefined lubricating oil, the tax exemption for the new oil was to be available only if 25 percent or more of the mixture consisted of waste or rerefined oil.

Revenue effects

Under H.R. 6860, it was estimated that the exemption from the 6-cents-per-gallon excise tax for lubricating oil mixed with waste or rerefined oil would reduce revenues by about $3 million per year. Under present law, revenue from this tax go into the Highway Trust Fund (through September 0, 1979).

Alternative proposals

Mr. Vanik

The excise tax disincentive for the use of rerefined oil would be removed (as was provided in H.R. 6860).

Mr. Rangel

The excise tax disincentive for the use of rerefined lubricating oil would be removed (as under H.R. 6860).

Mrs. Keys

The excise tax disincentive for the use of rerefined oil would be removed (as under H.R. 6860).

Areas for committee consideration

Both to further the nation's energy program and because of environmental considerations, the committee may wish to modify the excise tax provision in existing law which prefers the use of entirely new lubricating oil in nonhighway uses to the use of reclaimed and blended oil.

B. Repeal of Excise Tax on Radial Tires

Background

There are three basic tires produced by rubber fabricators: bias-ply, bias-belted, and radial. Radial tires have a greater useful life and perform better than other tires. In addition, use of radial tires are said to increase gasoline mileage by 3 to 5 percent. However, they retail for about double the price of typical bias-ply tires, but have a much wider profit margin. A large percentage of all radial tires sold in the United States are manufactured abroad.

Radial tires are now being installed on approximately 70 percent of all new cars assembled in the U.S., up from about 5 percent in 1972. In 1976, radials accounted for about 34 percent of the replacement market, and it is estimated by industry sources that they will account for approximately 40 percent of that market in 1977.

Present law

Present law imposes a manufacturers excise tax of 10 cents per pound on rubber tires of the type used on highway vehicles [1] and a manufacturers excise tax of 5 cents per pound on tread rubber.[2] Radial tires are taxed under these provisions according to the weight of the tire or the weight of the rubber used in retreading.

Administration proposal

The Administration proposal does not contain any provisions regarding the excise tax on radial tires.

Action in the 94th Congress

The House version of H.R. 6860 would have repealed the manufacturers excise taxes on radial tires,[3] and on tread rubber used to re-

[1] This tax is scheduled to drop to 5 cents per pound for sales on or after October 1, 1979. Under prior law, this tax was scheduled to be reduced as of October 1, 1977, but this date was extended by Public Law 94-280.

[2] This tax is scheduled to expire for sales on or after October 1, 1979. Under prior law. this tax was scheduled to expire on October 1, 1977, but this date was extended by Public Law 94-280.

[3] For purposes of these provisions, a radial tire was a tire of the type used on highway vehicles. in which the ply cords extending to the bead of the tire are laid at substantially 90 degrees to the center line of the tire tread. This is to distinguish such tires from "bias ply" tires, where the corresponding ply cords are laid at substantially 45 degrees to the center line.

cap or retread radial tires. This provision was adopted because the use of radial tires on highway vehicles was believed to reduce fuel consumption by 3 to 5 percent.

In addition, the bill provided for the retroactive refund of these taxes to dealers with respect to certain radial tires in their inventories.

The repeal of these taxes was estimated to reduce per-tire prices by an average of $3.

The Finance Committee bill did not include this provision.

Revenue effects

It is estimated that the repeal of the excise tax on radial tires would reduce revenues by about $336 million at 1977 levels, and $375 million at 1978 levels.[4] In addition, if the repeal of these taxes were made retroactive, it is estimated that this would result in an additional one-time revenue loss of $120 million. Under present law, revenues from these taxes go to the Highway Trust Fund through September 30, 1979.

Alternative proposals

Mrs. Keys

The excise tax on radial tires would be repealed.

Mr. Jones

The excise tax on radial tires would be repealed.

Areas for committee consideration

In considering the conservation impact of a repeal of the excise tax on radial tires, it should be noted that these tires are 3 to 5 percent more fuel efficient than other tires. However, radial tires are already being used on a majority of all new cars assembled in the United States and constitute a substantial part of the replacement market. Thus, it is altogether not clear if further incentives are necessary to encourage the use of radial tires.

Moreover, due to the great price differential between radial tires and other tires, the Committee may wish to consider whether the repeal of the taxes would affect the total cost of these tires sufficiently so as to encourage purchases of radial tires which would not have occurred in any event.

Another factor to be considered is the possible competitive impact of a repeal of these taxes on domestic tire manufacturers, since the percentage of their tire sales represented by radials varies considerably.

In addition, the Committee may want to consider the impact of a repeal of the tax on the Highway Trust Fund. Repeal of the tax on radial tires would involve an excise tax reduction of about $336 million based on 1977 levels and $375 million based on 1978 levels (or about $363 million for fiscal 1978 also, if the repeal were made retroactive there would be one-time revenue loss of another $120 million for fiscal 1978) and $400 million for fiscal 1979.

[4] If the tax on tires were not scheduled to be reduced on October 1, 1979, the revenue loss from the repeal of the tax on radial tires would increase about 10 percent per year due to growing use of radial tires.

If the Committee does decide to repeal these excise taxes, it may wish to consider the issue as to whether or not the repeal should be prospective or retroactive, i.e., whether the repeal should apply to existing floor stocks. If the repeal of these taxes is made retroactive, it is estimated that this would result in an additional one-time revenue loss of about $120 million. On the other hand, a prospective repeal might tend to discourage some consumers from purchasing radial tires until the dealers' current floor stocks are sold. However, a prospective repeal would avoid the administrative burden of refunding relatively small amounts of tax per sale and in determining and processing refund claims.

III. ENERGY TRUST FUND PROPOSALS

Background

Trust funds have been used in a variety of situations in conjunction with the imposition of various taxes. Generally, the proceeds of a particular tax, under the trust fund device, are designated for distribution to a trust fund. Revenues in the trust fund, in turn, are earmarked solely for specified expenditures. Ordinarily, the tax receipts otherwise would be includible in the general treasury, and would be available for any authorized expenditure. However, the trust fund normally will restrict the purposes for which its receipts can be expended to those specified in the legislation.

Perhaps the best known examples of special purpose trust funds are the Highway Trust Fund, the Airport and Airway Trust Fund, and the Social Security Trust Fund.

Present law

Under present law there is no energy trust fund. The Federal Government's energy expenditures are appropriated from the general revenues. In fiscal year 1976, the total Federal expenditures for energy research and development projects amounted to more than $1.7 billion.

Administration proposal

The Administration proposal does not contain any provision for the establishment of an energy trust fund.

Action in the 94th Congress

The Ways and Means Committee bill would have established an Energy Conservation and Conversion Trust Fund. This provision was adopted, with clarifying amendments, by the House.

Under the House bill, the trust fund would have received revenues from the import tariff and the tax on business use of petroleum and petroleum products.[1]

The House bill would have established specific limits on the amounts that could be appropriated to, or accumulated in, the trust fund. It would have limited the amount of the annual trust fund appropriation to $5 billion, and no more than $10 billion could have been accumulated in the trust fund at any one time. Any revenues raised in excess of these amounts were to be transferred to the general fund, as were any amounts remaining in the trust fund on its expiration date at the end of fiscal year 1985.

The House bill established four general categories of energy programs for which trust fund expenditures would have been author-

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[1] To the extent provided by subsequent legislation, the bill also would have permitted proceeds received by the United States Government from oil and gas properties in which the Government has an interest (for example, bonus payments and royalties received by the United States from leasing its lands and its rights for offshore drilling) to be included in the trust fund.

ized: (1) basic and applied research programs relating to new energy technology; (2) projects aiding in the development and demonstration of new energy technologies; (3) programs relating to the development of energy resources from U.S.-owned properties; and (4) research projects, or capital expenditures for demonstration projects, relating to local and regional transportation systems.

The emphasis of the first general category was to be on programs and energy technologies where the technical feasibility was sufficiently uncertain to prevent substantial private investment in research and development without financial assistance. The focus of expenditures within the second general category was to be on projects on which sufficient research had been completed to make technology of the product available, but for which some financial assistance was necessary to demonstrate or develop either the technology of production or the commercial feasibilty of the program or project. However, all amounts to be appropriated for any specific program (whether or not the programs were listed as examples in the legislation) were subject to the normal authorization and appropriations processes of Congress.

The House bill would have established a trust fund review board, the function of which would have been to make initial recommendations to Congress on how trust fund appropriations should be allocated among the four general categories for which expenditures were authorized. In addition, the board was to conduct an annual review of the effectiveness of trust fund expenditures. Members of the review board were to be appointed by the President with the advice and consent of the Senate, and were to be subject to strict conflict-of-interest regulations.

In its initial consideration of H.R. 6860, the Senate Finance Committee tentatively agreed to delete the Energy Trust Fund from the House bill and to substitute for it an Energy Development Loan Guarantee Fund to encourage the commercial development by private industry of new and alternative energy sources. However, this provision was not included in the energy provisions as reported by the Committee.

Under the Finance Committee's tentative decision, eligible projects would have included the production of energy from organic solid wastes, the production of other synthetic fuels, such as gasified coal, liquified coal, oil shale and tar sands, and the production of components and systems for sale to the public to heat and cool buildings with solar energy (nuclear projects were excluded). Eligible beneficiaries would have been required to provide at least 20 percent of the cost of the project and could obtain loan guarantees for the remaining 80 percent. No new loan guarantee could be undertaken after December 31, 1980, and the total loans guaranteed in any fiscal year could not exceed $2.5 billion. Under the Finance Committee's tentative decision, loans in excess of $100 million could not be guaranteed unless the Congress were notified in writing and neither House of Congress adopted a resolution of disapproval within 30 days. The loan guarantees were to be backed by receipts from existing tariffs (or tariffs that might otherwise be provided in the bill) of 10 cents per barrel of oil, plus loans from the general fund, if needed.

Alternative proposals

Mr. Waggonner

A trust fund would be created from any standby gasoline tax revenues to fund energy research and development, oil and gas exploration, stocking of strategic petroleum reserves and mass transit development.

Mr. Steiger

An "energy account" would be established, with any excise taxes placed in the account to fund energy research and development, railroad redevelopment, mass transit (including buses), tax incentives for the construction of shale oil facilities and coal liquefaction and gasification facilities, and the acquisition of a billion barrel oil reserve.

Mr. Schulze

An energy trust fund would be created for 5 years (phasing out over an additional 5 years) with the funds used for new energy technology research programs and demonstration projects, the development of energy resources on U.S.-owned property, mass transit research and construction projects, hydroelectric plant development, and home insulation and other kinds of home conservation devices.

Areas for committee consideration

The basic issue for the committee to consider is whether to tie spending for research, development, and demonstration projects in the energy area to the revenues collected from specific taxes. A wide variety of programs in these areas already exists, and it is not clear under what circumstances the appropriate budget in this area would exactly correspond to tax collections.

If the committee decides to consider the creation of an energy trust fund, it should examine the provisions of H.R. 6860 (summarized above) which would have created such a fund. In the event that it decides to create an energy trust fund, the committee might wish to circumscribe its operation and expenditures in a manner similar to that provided for in H.R. 6860. The programs for which expenditures are authorized could be set forth in general terms, and probably should not be duplicative of current appropriations programs, except to the extent that Congress desires to increase expenditures in a particular area. In addition, the projects or programs for which expenditures are made or authorized might be made subject to Congressional review, as well as to evaluation by a specially instituted review board, with the advice of the Secretary of Energy and of any other departmental official into whose jurisdiction a particular expenditure otherwise might fall.

Moreover, both the duration and the assets of the trust could be limited. If Congress, thereafter, desires to extend the trust fund or to modify the amount of its funding, it could do so after an appraisal of the efficacy of the overall trust program. In the interim, the trust fund might be given additional appropriations if necessary, but probably should not be allowed to retain an idle, yet earmarked, revenue surplus.

If the committee does decide to create an energy trust fund, there are a number of possible sources of revenues which might be available for such a fund. For example, if the committee decides to adopt the tax on fuel inefficient cars, but not to adopt the rebate proposal for fuel efficient cars suggested by the Administration, those revenues could be earmarked for the trust fund. In addition, the committee might consider earmarking some fraction of the revenues from the crude oil equalization tax for the trust fund. Also, if the committee decides to impose tax on industrial and utility use of oil and natural gas, but not to adopt the credit proposed by the Administration in connection with the tax, this would be another possible source of revenues. Finally, if the committee should decide to impose additional import duties, these revenues could also serve as a basis of funding for the trust fund.

There is, of course, a great deal which could be done with the trust fund revenues at the Federal level in terms of funding projects for energy research and development. However, the committee might also wish to consider the possibility of distributing some of the revenues to State and local governments in connection with energy savings programs to be conducted at those levels. (This would constitute a form of energy-related revenue sharing.)

If the committee did decide to allow some of the money to be channeled to State and local governments, it might wish to prescribe certain categories of activity which would receive the highest priority in terms of receiving grants from the fund. For example, if the committee decided to encourage car pooling, it could provide that this would be a high priority category. Thus, grants might be made to local governments which establish special car pooling lanes or provided special downtown parking facilities for individuals who participated in car pools. Or, the committee might provide that grants for public transportation would be made available to local governments which imposed a substantial parking tax with an exception for participants in a car pool.

The use of the trust fund to encourage car pooling, is, of course, only one example of the way in which the trust fund could be used to encourage State and local energy saving programs. There are doubtless many other programs which could be similarly encouraged by providing that local governments which created adequate programs of energy savings would be entitled to receive grants from the trust fund. The committee might wish to consider establishing a procedure whereby State and local governments would present programs for review by the Secretary of the Treasury, in consultation with the FEA. The committee also may wish to specify certain programs which would receive priority and some of the criteria which the Secretary of the FEA should weigh in considering grant applications from State and local governments.

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