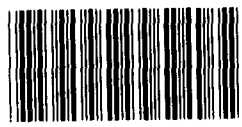
120806

24568

UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

For Release at 9:30 a.m.
March 7, 1983

STATEMENT OF
F. KEVIN BOLAND
SENIOR ASSOCIATE DIRECTOR
RESOURCES, COMMUNITY AND ECONOMIC
DEVELOPMENT DIVISION
BEFORE THE
SENATE COMMITTEE ON ENERGY AND
NATURAL RESOURCES



Mr. Chairman and Members of the Committee:

We appreciate the opportunity to be here today to discuss the Nation's preparedness for dealing with energy supply disruptions. GAO has done a substantial amount of work in this area during the past few years. This work includes a series of reports, requested by the Chairman and several Members of this Committee, that evaluate administration documents submitted to the Congress under the Energy Emergency Preparedness Act of 1982 (EEPA). Among these documents are a Memorandum of Law setting forth legal authorities available to the President to respond to a severe energy supply shortage, two documents detailing how the administration would use the Strategic Petroleum Reserve (SPR) in an emergency, and a "Comprehensive Energy Emergency Response Procedures Report" describing the options the President would consider using in an emergency and the procedures to implement them.

If I may briefly summarize our findings on these documents:

1. The Memorandum of Law discusses the individual statutes available to the President in various oil emergencies. The President has different statutory authorities, many of which are not specifically targeted to cope with oil emergencies. These actions taken to respond to a particular oil emergency will have to comply with different

legal requirements. In addition, gaps may exist in the authorities available to the President to deal with these emergencies.

2. The two SPR use planning documents provide little specific information about the conditions in which SPR oil could be used in an emergency, including the amount, rate, and timing of its use. Furthermore, neither document deals with important policy questions, such as the possibility that some SPR oil might be retained in private inventories after it is sold.

3. The comprehensive procedures report does not adequately describe specific options to be considered along with related implementing procedures. In addition, statements in the report, as well as recent and ongoing GAO work in this area, demonstrate that key components of the administration's energy emergency preparedness program are still inadequate.

I will discuss these findings in more detail. Before doing so, however, I would like to talk about Strategic Petroleum Reserve issues and concerns. At the present time, the SPR is the only real option available to cope with a major supply disruption.

SPR fill rate

Over the last two years, the administration has made good progress in filling and expanding the SPR. About 185 million barrels of crude oil were added to the SPR over fiscal years 1981 and 1982. The annual fill rate peaked at 292 thousand barrels a day (MBD) during fiscal year 1981 and dropped to 214 MBD in fiscal year 1982. The Energy Emergency Preparedness Act of 1982 requires a minimum average annual fill rate of at least 300 MBD until there are 500 million barrels in the Reserve. However, if the President finds for any fiscal year that this rate is not in the national interest, the minimum fill rate becomes 220 MBD or the highest practicable rate achievable subject to the availability

of funds. In 1983 the administration expects to fill at the rate of 220 MBD.

The administration's proposed fill rates for fiscal years 1984 through 1986 are considerably below 220 MBD and delay by about 2 years the achievement of a 500 million barrel reserve. The proposed fill rates for fiscal years 1984 through 1986 would not even fill available permanent storage capacity. Attachment I summarizes the oil fill and storage capacity estimates implied by the President's budget.

Under the administration's plans for fiscal year 1984, the average fill rate would be about 145 MBD--less than half of the required 300 MBD rate. If the administration maintains its current permanent storage expansion plan, this fill rate would result in nearly 18 million barrels of unused permanent storage capacity by the end of fiscal year 1984. (See Attachment I.) If this additional capacity were filled during the year, the average fill rate could be increased from 145 MBD to about 190 MBD.

Projected oil purchases and prices for fiscal years 1985 and 1986 contained in the administration's fiscal year 1984 Budget imply that the administration plans to fill the SPR at a rate of 100 MBD in those 2 years. This fill rate is about one-third of the required 300 MBD rate and would result in unused storage capacity of over 26 million barrels and 55 million barrels in fiscal years 1985 and 1986, respectively.

Slowing the fill rate will extend the time needed to achieve a 500 million barrel reserve by about 2 years. In establishing

the minimum fill rate requirements of the Energy Emergency Preparedness Act, the Congress demonstrated the importance it attached to filling the SPR to a minimum 500 million barrel level. Maintaining a minimum fill rate of 300 MBD after fiscal year 1983 would allow this goal to be reached by January 1985. Lowering the post-fiscal year 1983 fill rate to 220 MBD would delay reaching this target until July 1985. By our calculations, the administration's proposed and implied fill rates of 145 MBD in fiscal year 1984 and 100 MBD thereafter would delay reaching this goal until March 1987 (See Attachment II).

The administration's budget proposal would also delay construction of permanent storage needed for the final 150 million barrels of the planned 750 million barrel reserve. Specifically, the administration has proposed this year to defer funds, as it did in fiscal year 1982, for the development of the Big Hill, Texas site. In addition, the fiscal year 1984 budget contains no funds for construction at Big Hill. The budget states that "a decision on whether to proceed with construction on this site will be reanalyzed in the context of the 1985 budget."

SPR drawdown plans

The protection from the adverse effects of supply disruptions provided by the SPR is largely determined by how quickly the Government can distribute the proper amount of SPR oil. Advance planning for SPR use is crucial to the Government's ability to act quickly, possibly at the outset of a supply disruption. Advance SPR use planning also shows oil consumers that drawdown has been effectively planned and so reduces panic buying that contributes

to oil price increases in a disruption. It also allows the Government to more easily coordinate stock drawdown with our allies, while it deters oil embargoes against the United States by demonstrating our ability to counteract one.

While SPR use planning is clearly advantageous, we pointed out in past reports and testimony that the administration has not adequately addressed many crucial policy questions of when and how the SPR should be used. The administration's recently issued SPR Drawdown Plan and SPR Drawdown and Distribution Report, which we evaluated in our January 1983 report to this Committee, provide little specific information about SPR use in an emergency, including the amount, rate, and timing of its use. In addition, neither of these documents deal with important policy questions such as the possibility that some SPR oil might be retained in private inventories after it is sold. As our experience in the 1979 Iranian oil supply interruption demonstrated, it is conceivable that buyers, anticipating rising oil prices during an emergency, may choose to hold on to their oil longer.

In our view, the administration needs to do more analysis and provide more policy guidance on such questions as the timing of SPR drawdown, optimum drawdown strategies in various types of disruptions, and how it will coordinate stock drawdown with other countries. Current research shows that early drawdown is crucial to minimizing price increases from disruptions, but there are circumstances where national security or other factors could suggest later drawdown. Current SPR use plans do not consider or evaluate these tradeoffs or draw conclusions.

The degree to which SPR use is effective depends on a number of variables. For example, it can be made more or less effective depending on such factors as oil inventory levels, consumption, production, and price movements when a disruption occurs. More analytical work on these factors is required to provide a solid basis for good policy decisions on how and when to use the SPR.

Current research also shows that the effect of the SPR on world oil prices depends on other nations' stock policies. If other nations build stocks during disruptions, the effects of SPR drawdown would be blunted, while coordinated drawdown would greatly enhance the effects of the SPR. While the Department of Energy has funded some research on this, it has not, to our knowledge, developed practical plans to coordinate stock drawdown with our allies.

In addition to insufficient analysis in these areas, the administration seems reluctant to state SPR use policies. The administration has stated that it objects to specifying SPR use policies in advance because of: (1) uncertainties about the circumstances of a disruption, (2) the need to preserve Presidential flexibility, and (3) the need to keep sensitive information secret. We do not believe these are valid reasons for avoiding advance planning. Since uncertainties will also exist during disruptions, advance planning could assist decisionmakers by providing the analytical basis for responding more rapidly and effectively to changing conditions. Furthermore, flexibility can be preserved by detailing options rather than prescribing a single plan. The need for secrecy can be preserved by developing plans

but not releasing sensitive contents to the public, as is done in military contingency planning.

COMPREHENSIVE ENERGY EMERGENCY PLANNING

The administration's Memorandum of Law and Comprehensive Energy Emergency Response Procedures Report address a broad range of energy emergency preparedness programs and issues, including the SPR. The Memorandum of Law was required by EEPA to describe the nature and extent of the authorities available to the President under existing law to respond to energy emergencies. The procedures report was to describe the options the President would consider using to implement these authorities, specify how potential response actions would be selected and implemented, and recommend additional laws that the President may need to deal with an emergency.

Memorandum of Law

The Department of Justice's memorandum discusses the individual statutes available to the President in various oil emergencies. It discloses that the President has different statutory authorities, many of which are not specifically targeted to cope with oil crises. The different statutes do not use common terms or language to trigger their authorities. Thus, actions taken to respond to a particular oil crisis will have to comply with a number of different legal requirements. For example, a particular crisis may fit the statutory conditions for a "severe energy supply interruption" under the Energy Policy and Conservation Act, but may not amount to a defense-related emergency under the Defense Production

Act. This would mean that the President would have authority to establish demand restraint measures under EPCA, but could not use the Executive Manpower Reserve, which is available only in defense-related emergencies.

What emerges from this mosaic of statutes are gaps in the authorities available to the President to cope with oil crises. Many have noted the lack of a provision preempting State and local petroleum allocation and price control laws. The Emergency Petroleum Allocation Act of 1973 contained Federal authority to preempt such laws, but that Act expired in 1981. This omission may set the stage for litigation at the beginning of a crisis to establish the scope of Federal preemption of State and local regulatory activities. Secondly, oil industry lawyers question whether the President has clear authority to implement a domestic fair sharing system to carry out U.S. obligations under the International Energy Program. Furthermore, provisions of the SPR Drawdown Plan may preclude use of most SPR oil to meet these obligations.

The Comprehensive Procedures Report

The comprehensive procedures report does not adequately deal with the emergency response options available to the President or the procedures to implement them. The options are inadequately detailed and some face implementation problems. Also, the procedures lack necessary detail, and many of them have not yet been fully developed.

"Options" are inadequately detailed and some face implementation problems

Key program and policy options mentioned in the report include the SPR, the Emergency Executive Manpower Reserve, international energy programs, private oil stocks, and possible Federal preemption of State laws and regulations. As noted in our earlier discussion of the SPR, the administration has not yet effectively planned for its use, and plans to substantially slow its fill rate and capacity expansion. In addition, procedures for drawdown and distribution need to be tested (such a test is scheduled for July 1983) and several legal issues identified in our January report should be resolved to facilitate the distribution of SPR oil.

According to the procedures report, another major program the administration intends to use to respond to a severe energy emergency is the Emergency Executive Manpower Reserve. The objective of this program is to use experienced industry personnel who can help identify and assess supply and demand problems and assist in coordinating energy production and distribution during energy emergencies.

While this is a potentially useful program, the administration has not resolved legal problems that could prevent its effective use. Using Reservists to help manage Federal energy programs during supply disruptions presents potential conflict-of-interest problems. Reservists are subject to the same conflict-of-interest laws as all Federal employees. This is of particular concern because criminal penalties are imposed on any Government employee who participates

in areas where he has financial or employment-related interest. In addition, reservists are subject to additional conflict-of-interest provisions of the Department of Energy Organization Act. This act would in some circumstances require reservists to divest themselves of financial holdings in any energy concern, and it prohibits any official relation with an energy concern by a supervisory employee of the Department of Energy. Furthermore, if private industry personnel from various companies work together, there are potential antitrust concerns. Finally, the Reserves can be activated only in defense-related circumstances.

The administration acknowledges the existence of both conflict-of-interest and antitrust problems, and notes that they impeded use of the reserves during the 1973 Arab oil embargo. However, it has no current plans to propose legislation to alleviate these concerns. The Department of Energy's Deputy Assistant Secretary for Energy Emergencies told us that it is unlikely that specific proposals would be made before 1984. In our view, the administration may not be able to effectively use the Emergency Executive Manpower Reserve if the disruption occurs before such legislation is enacted.

The procedures report also identifies several international energy programs relating to U.S. obligations as a member of the International Energy Agency (IEA) and the North Atlantic Treaty Organization (NATO). Little detail is given on the content and status of these programs. In addition, recent GAO work in this area has shown that the Government lacks effective procedures under which U.S. oil companies may participate in the IEA Emergency Sharing System with limited antitrust protection during an

actual emergency; there are virtually no standby demand restraint programs in place which may be needed to comply with IEA requirements; and there are differences among Agency member countries over prices charged for oil shared under the Emergency Sharing System. In addition, GAO is reviewing possible coordination problems in an energy emergency because of both IEA and NATO treaty commitments along with a followup review of U.S. participation in the IEA in general.

The procedures report asserts that private oil stocks would play a major role in coping with oil supply disruptions and that private and Government stocks currently provide substantial protection against such disruptions. However, the administration does not appear to have decided on the role of private stocks or how to ensure that adequate levels are maintained and drawn down during disruptions. While the report states that private stocks are currently at high levels, it does not mention the decline in stock levels over the past year, or the fact that most of these stocks are needed for operations, and thus cannot be used for emergency drawdown.

Furthermore, the report does not address how the Government might encourage industry to maintain adequate stock levels and draw them down during disruptions. This is of particular concern since a recent Department of Energy-funded study concluded that the reduction in inventory levels has run counter to public sector efforts to increase inventories and that "even moderate panic buying will produce a demand for products that could overwhelm the capacity of the industry to respond." In our view, the admini-

stration cannot count on private stock drawdown to mitigate the effects of a disruption. In fact, oil companies may continue to build stocks during disruptions, as has been observed in past disruptions.

A key problem only briefly discussed in the procedures report is the potential conflict between Federal and State laws and policies. As we noted earlier, individual States could enact petroleum allocation and pricing laws or other regulatory measures which would be at variance with the administration's free market approach. In fact, about 20 States have oil set-aside or other types of fuel management plans such as rationing, which may be inconsistent with the Federal approach.

The administration alludes to this problem, stating in the procedures report that in a severe emergency, the Federal Government "may attempt to dissuade the States from taking regulatory actions which conflict with the Federal market strategy." However, the report does not present any possible measures of dissuasion nor does it address the difficulty of litigating, in emergency circumstances, the principles of preemption of State allocation and price controls. In its legal memorandum, the Department of Justice acknowledged that it would be difficult to preempt these types of State laws and regulations.

Emergency response procedures are vague and are not fully developed

Beyond the concerns we have raised about the response options identified in the procedures report, the report does not demonstrate that reliable emergency response procedures are available

to implement these options. Section 272(b)(2)(B) required the report to

> "* * *specify how appropriate governmental actions in response to international and domestic energy shortages would be selected and implemented under such options, particularly which official Governmental entity would select and implement such actions, and what procedures would be used in doing so."

However, while the report indicates who the major participants are, including DOE offices, other agencies, and interagency groups, the eight pages specifically devoted to "emergency response procedures" give little detail on how Government response options would be selected and implemented, which individuals or groups make key decisions or select response options, how specific organizations would coordinate their activities, and what implementation procedures would be used by each participating group for different response actions. Another problem with the procedures is that they are not finished. For example, the procedures report acknowledges that detailed procedures have not yet been developed to implement many of the response options we discussed earlier. The report states that "for each of these programs, the DOE is either currently developing detailed procedures * * * or is studying possible measures that might have potential, or is doing both."

- - - - -

In summary, we would like to re-emphasize a few key points about how we view the administration's readiness to respond to an energy emergency, as reflected in the documents required by EEPA:

--While the administration has made good progress on filling the SPR in the past, its proposed fill rates

for fiscal years 1984 through 1986 delay by about two years the achievement of a 500 million barrel reserve. The administration's proposed budget would also delay construction of some permanent storage.

--The administration has not adequately addressed the crucial policy questions of when and how to use the SPR, limiting its ability to counter the adverse effects of disruptions. Questions not adequately addressed include the timing of SPR use, how to use the SPR most effectively under different types of disruptions, and how to coordinate stock drawdown with other countries.

--The President has different statutory authorities to respond to energy emergencies, many of which are not specifically targeted to cope with such emergencies. Thus, actions taken to respond to particular oil emergencies will have to comply with different legal requirements. In addition, gaps may exist in the authorities available to the President to deal with these situations.

--The emergency response options available to the President are inadequately detailed in the comprehensive procedures report and some face implementation problems. Among our specific concerns:

  --Key programs, notably the Strategic Petroleum Reserve (SPR), Emergency Executive Manpower Reserves, and some International Energy Agency programs face major implementation problems.

  --Key policy issues in some program areas (for example, coordination of Federal and State policies and programs) are not adequately resolved.

  --Some key issues, such as the role of private stocks, are barely discussed or are omitted altogether.

--The procedures report does not demonstrate that reliable emergency response procedures are available to implement the above options. Specifically:

  --The descriptions of the roles of decisionmakers, and those implementing their actions, lack necessary detail. As a result, the procedures to be followed within the Department of Energy and other organizations and among agencies are not clear.

--Many of the procedures have not yet been fully developed.

- - - - -

That concludes my prepared testimony. We would be happy to respond to any questions.

ATTACHMENT I

SPR OIL FILL AND STORAGE CAPACITY ESTIMATES

BASED ON THE BUDGET PROPOSAL

	FY 1983	FY 1984	FY 1985	FY 1986
Average fill rate (MBD)	a/ 216	145	100	100
Total fill (million barrels)	357	410	446	483
Total capacity (million barrels)	357	b/ 428	b/ 473	c/ 538
Unused capacity (million barrels)	--	18	27	55
Average fill rate if excess capacity used (MBD)		190	123	179

---

a/The FY1984 Budget calls for an average fill of 216 MBD; however, the Department of Energy now plans to fill at an annual average rate of 220 MBD.

b/Revised capacity estimates per the Department of Energy.

c/Previous capacity schedule.

ATTACHMENT II

SPR OIL FILL SCHEDULES TO ACHIEVE 500 MILLION BARRELS IN STORAGE (note a)

(millions of barrels)

Fiscal year	Assuming FY 1984 budget fill rates b/	Assuming permanent storage capacity is filled	Assuming 220 MBD fill rate	Assuming 300 MBD fill rate
1983	c/ 357	357	358	d/ 358
1984	410	428	439	468
1985	446	473	e/ 500	e/ 500
1986	483	e/ 538		
1987	e/ 519			

---

a/There were 278 million barrels in storage at the end of fiscal year 1982.

b/Assuming fill rates of 216 MBD in FY 83, 145 MBD in FY 84 and 100 MBD thereafter.

c/The Department of Energy now expects to fill at a 220 MBD rate in fiscal year 1983.

d/On December 1, 1982, the President found that it is not in the Nation's interest to fill the SPR at a rate of 300 MBD in fiscal year 1983. The Administration has not determined what is the highest practicable fill rate, but currently it plans to fill the SPR at a rate of 220 MBD.

e/500 million barrel reserve reached in March 1987 at budgeted fill rate, February 1986 if available capacity filled, July 1985 if filled at 220 MBD, and January 1985 if filled at 300 MBD.