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STATEMENT OF
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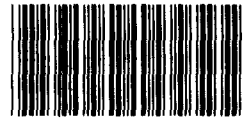
BEFORE THE
SUBCOMMITTEE ON FOSSIL AND SYNTHETIC FUELS,
HOUSE COMMITTEE ON ENERGY AND COMMERCE

Mr. Chairman and Members of the Subcommittee:

We appreciate the opportunity to be here today to discuss issues of concern about the Strategic Petroleum Reserve (SPR). Because of the vital role the SPR plays in protecting our Nation's security and economic health during oil supply disruptions, GAO has done a substantial amount of work on the SPR. We issue quarterly reports on the SPR's status and have recently issued a report evaluating the Administration's SPR drawdown plans for the Senate Committee on Energy and Natural Resources. We also have done substantial analysis of the Administration's overall emergency preparedness program. We will soon be issuing a report which assesses the Administration's Comprehensive Energy Emergency Response Procedures, including those relating to the SPR. Our comments today are primarily based on this work and will cover the SPR budget, including funding for both oil acquisition and expansion of storage capacity, the Administration's SPR drawdown plans, and its overall energy emergency preparedness program.

Two problems that plagued the early development of the SPR were delays in construction and oil acquisition. Over the last 2 years, the Administration has made good progress in filling



and expanding the SPR. However, the Administration is currently reducing its fill effort, because of budgetary concerns and the improved energy supply situation. From a contrasting viewpoint, however, the current energy supply situation and the related softness in oil prices make this an ideal time to purchase additional oil for the SPR. Two specific areas of concern about the Administration's SPR plans, as contained in the fiscal year 1984 budget, are that the fill rates proposed for fiscal years 1984 through 1986 will not use all available permanent storage capacity and that planned capacity expansion is being delayed. Additionally, our evaluation of the Administration's SPR documents recently submitted to the Congress shows that little progress has been made in planning for SPR use. The status and readiness of the SPR are particularly important, Mr. Chairman, because the Administration has few other programs that can be implemented in an energy emergency. The SPR is the cornerstone and by far the largest element of the Administration's energy preparedness program.

SPR FILL RATE

About 185 million barrels of crude oil were added to the SPR over fiscal years 1981 and 1982 bringing the total amount of oil in the Reserve to 278 million barrels. 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.

The Administration's proposed fill rates further delay completion of the SPR

The Administration's proposed fill rates for fiscal years 1984 through 1986 are disappointing and delay by at least 2 years the achievement of a 500 million barrel reserve. The proposed fill rates for fiscal years 1984 through 1986 would not fill permanent storage capacity and fall below the minimum 220 MBD of the Energy Emergency Preparedness Act. The rate of 220 MBD, it should be noted, would require the use of interim storage starting in fiscal year 1984. This was authorized by the Energy Emergency Preparedness Act. Attachment I summarizes the oil fill and storage capacity estimates implied by the President's budget.

In the first quarter of fiscal year 1983, the Administration filled the SPR at an average rate of 173 MBD. While, the President's budget states that the average fill rate over the entire fiscal year would be 216 MBD, we understand that the Administration intends to revise that rate to 220 MBD.

Under the Administration's plans for fiscal year 1984, the average fill rate would drop to about 145 MBD or less than half of the required 300 MBD rate. This proposed fill rate for fiscal year 1984 is disappointing in terms of what it could be if all available permanent storage capacity were used. 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 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. 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.)

Legal issues surrounding proposed fill rates

On December 1, 1982, the President declared that it would not be in the national interest to fill the SPR at the 300 MBD rate in fiscal year 1983, so the minimum statutory fill rate became 220

MBD or the highest practicable fill rate achievable. Whether the Administration is required to fill at a rate above 220 MBD depends in the first instance on the availability of funds. Under the Energy Emergency Preparedness Act, there is a legal issue, which we have not yet resolved, concerning how much of SPR funding is to be deemed available for purposes of computing the minimum fill rate. We are presently reviewing this matter as well as others concerning the interpretation and implementation of the Energy Emergency Preparedness Act's fill rate requirements. We will report to the Subcommittee soon on these matters.

You also asked us whether the Department of Energy is in violation of the Impoundment Control Act by filling the SPR at an average daily rate lower than that which available funds would support. The Impoundment Control Act requires the President to report to the Congress when he proposes to defer budget authority. In this case, if the Administration fills the SPR at a rate below the highest practicable rate achievable, one consequence of such action is that the difference between the funds required for the actual fill rate and the funds needed to achieve the highest practicable fill rate should be reported to the Congress under the Impoundment Control Act.

DELAYS IN CAPACITY EXPANSION

The Administration has taken actions which would delay construction of the final 150 million barrels of the planned 750 million barrel reserve. The previous Administration planned

on achieving a 750 million barrel reserve by 1989. Last year the current Administration moved the completion date back to 1990. Current budget plans would delay reaching this goal by at least another year.

In fiscal year 1982, the Congress rejected the Administration's attempt to defer $53 million for development of the new Big Hill, Texas site, which contains most of the last 150 million barrels. This year the Administration again proposes to defer funds for the development of Big Hill in the amount of $57.4 million. The Administration acknowledges that, "this deferral will result in some delay in the completion of the 750 million barrel reserve," although it does not specify the length of the delay. In addition, the fiscal year 1984 budget contains no funds for construction at Big Hill.

The Administration maintains that it is committed to achieving a Reserve of 750 million barrels. However, the Administration has deferred the decision of whether to develop the Big Hill site until next year. The President's budget stated that "a decision on whether to proceed with construction on this site will be re-analyzed 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 our September 1981 report, 1/ in previous testimony, 2/ and again in our January 1983 report, 3/ that the Administration has not adequately addressed the crucial policy questions of when and how the SPR would be used. The Administration's recently issued SPR Drawdown Plan and SPR Drawdown and Distribution Report, which we evaluated in our Janaury 1983 report to the Senate Committee on Energy and Natural Resources, 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.

In our view, the Administration needs to do more analysis and provide more policy guidance on such questions as the timing

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1/"The United States Remains Unprepared for Oil Import Disruptions," EMD-81-117, Sept. 29, 1981.

2/Statement of Donald Z. Forcier, Senior Group Director, Energy and Minerals Division before the Senate Committee on Energy and Natural Resources, May 6, 1982.

3/"Analysis of the Strategic Petroleum Reserve Drawdown Plan and the Strategic Petroleum Reserve Drawdown and Distribution Report," GAO/RCED-83-85, Jan. 3, 1983.

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 the price increase from the disruption, but there are circumstances where national security or other factors would 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 the status of 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 nation's 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.

OTHER EMERGENCY PREPAREDNESS ISSUES

The SPR must be viewed in the context of the Administration's other energy emergency planning activities to get a complete picture of the Nation's preparedness for future disruptions. We examine these activities for our forthcoming report to the Senate Committee on Energy and Natural Resources evaluating the Administration's Comprehensive Energy Emergency Procedures report. The Administration has stated that the Emergency Executive Manpower Reserve and private oil stocks are important buffers to the adverse effects of energy supply disruptions. However, because of legal difficulties in effectively using the Emergency Executive Manpower Reserve and because the Administration has no plans to encourage private oil stock drawdown during disruptions, the Administration has little more than the SPR to deal with supply disruptions. In addition, the Administration appears to be doing little to resolve potential conflicts between Federal and State policies that could arise in disruptions.

One of the major programs 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 energy industry personnel 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 an employee of the Department of Energy who has a managerial role. 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.

While the Administration acknowledges the existence of both conflict-of-interest and antitrust problems, 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 Administration asserted in the Procedures report that private oil stocks and the SPR, taken together, are a sufficient buffer to the adverse effects of supply 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 Administration 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.

Another key problem with the Administration's energy emergency plans is the potential conflict between Federal and State laws and policies. 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, our research shows that presently 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 its recent 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. The Emergency Petroleum Allocation Act of 1973 contained Federal authority to preempt State allocation and price controls, but that law expired in 1981. In its legal memorandum required by the Energy Emergency Preparedness Act, the Department of Justice acknowledged that it would be difficult to interpret another statute in a manner that would authorize preemption of these types of State laws and regulations.

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In summary, we would like to re-emphasize a few key points about how we view the Administration's SPR plans:

--While the Administration has made good progress on filling the SPR in the past, its proposed fill rates for fiscal years 1984 through 1986 will not even fill permanent storage capacity and will delay by 2 years the achievement of a 500 million barrel Reserve.

--The Administration's proposed fill rates for fiscal years 1984 through 1986 are below the 300 MBD and the possible 220 MBD minimum rates set forth in the Energy Emergency Preparedness Act of 1982. Interim storage would be required to achieve even the lower rate.

--The Adminsitration is also delaying by at least 2 years construction of the last 150 million barrels of the planned 750 million barrel Reserve, by not funding construction at the Big Hill, Texas site.

--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 status and effectiveness of the SPR are crucial to our ability to deal with an oil disruption, since it is virtually the only major mechanism available at the present time. Other potential mechanisms, such as the Emergency Executive Manpower Reserve and the use of private stocks, have implementation problems or are otherwise unreliable.

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That concludes my prepared testimony, Mr. Chairman. 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

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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			

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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.