Statement of the American Petroleum Institute
Submitted to
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Committee on Government Affairs
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The American Petroleum Institute (API) is pleased to have the opportunity to present a statement on the oil supply situation in the United States, and on the impact of rising prices on consumers of petroleum products. API represents nearly 500 companies engaged in all aspects of the U.S. oil and natural gas industry, including exploration, production, refining, distribution and marketing.

At the outset, we wish to emphasize that America's oil and natural gas industry is committed to continue supplying American consumers with a reliable and affordable supply of energy for all their needs. We also pledge to provide consumers with the information they need about the current gasoline price situation and any concerns regarding fuel supply.

We share your concern about the current oil supply situation, and your desire to reduce its impact on your constituents. We are taking what actions we can to improve conditions, and also have suggestions to offer for actions that can be taken by government and by consumers themselves.

Let me take a moment to frame the situation. Contrary to the views of some, the age of petroleum is far from over. While research and development continue on alternative sources of energy, gasoline and diesel fuel remain the most cost-effective and prevalent fuels for our transportation needs. To be specific, 97 percent of all transportation is fueled by petroleum products. These fuels, and the infrastructure built to fuel a nation of cars and trucks, allow us to get to where we need to go. Whether we need to go to work, take a school bus, get produce to market, or fly for business or pleasure, oil plays a crucial role in our daily lives – and will continue to do so for decades to come.

Four important points should be understood about the current situation:

- First, prices at the gasoline pump are determined by the cost of crude oil, and crude oil prices are determined by supply and demand in the international marketplace.

- Second, high crude oil prices have resulted from a decrease in foreign oil production and a greater demand for oil from the recovering Asian economies and a continued growth of Western economies.

- Third, although prices have risen rapidly, retail prices, after adjusting for inflation, are generally well below the prices of the early 80s.

- Finally, the U.S. oil and natural gas industry is operating its refineries at record production levels – within safety and environmental limits - and will continue increasing as we approach the prime drive season when the demand for gasoline is at its highest.

Let me address these points in more detail:

The price increases we are experiencing were brought on by short-term shocks that resulted from sudden changes in supply and demand. Just as prices are up now, they will turn down when factors change. Already, the price of crude oil has dropped $5.00 over the past several weeks.

In a free-market economy, we have seen time and again that price movements ultimately create balance between supply and demand. We are confident that if we continue to allow the marketplace to work, this balance will be maintained. And, history shows us that the longer-term cost of the product is less than otherwise would be the case.

The U.S. oil and natural gas industry can best provide American consumers with a steady and affordable supply for all their needs when markets are allowed to function as freely as possible. We commend the federal government for taking a balanced approach to the current situation by encouraging more foreign crude oil production while refraining from interfering in the marketplace, which is still the best way to get gasoline to consumers, reliably and at the lowest cost.

The past 15 months have seen us go from a period of extremely low prices to a peak where crude oil prices have reached levels that were three times those of the previous year. This dramatic change in crude oil prices has contributed to increases in the prices for petroleum products of about 70 percent. These changes have made it difficult for consumers to plan and budget for expenditures and have absorbed a larger share of family incomes.

These changes were brought on by increases in world demand for petroleum due to robust growth in world economies and reductions in supply by foreign oil producing nations. World petroleum stocks have been drawn down, and prices have been driven up.

Despite the limitations on world supplies, our companies are working hard to produce all the gasoline and diesel fuel that our customers will need during the coming months. Refinery output of gasoline and distillate oil set records for the month of February, and distillate oil production may set a record for this heating season.

A fair question is: “How did we get to this point?”

The answer is relatively straightforward. We have experienced twenty years of more and more overlapping regulations that have left our nation’s petroleum distribution system with minimal flexibility. Restrictions on producing petroleum in this country have led to declines in domestic production by one third over the past three decades. We now import about 55 percent of our petroleum needs. This large demand on foreign supplies leaves us at the mercy of world supply and demand conditions and open to the volatility that we have experienced over the past year.

I would like to share with you how our companies are striving to supply products to consumers:

Refinery processing of crude oil is above average and set a record in 1999.

Refinery production of gasoline set a record for the month of February. It was 14 percent above average, approximately about one million barrels more per day.

Refinery production of distillate oil (such as heating oil and diesel fuel) set a record for the month of February as well. It is on pace to set a record for this heating season.

Refinery utilization is currently above average for this time of the year and exceeded 90 percent last week.

These measures indicate that our industry is working as hard as possible to safely deliver the products that consumers need. It is also important to note that while world supplies are reduced, there are no shortages at the present time. Because of the world prices for crude oil, we are faced with higher product prices, however all customers are being served.

Given these conditions, what should be done?

What government can do

The most important action that the government can take is to provide information to citizens on petroleum market conditions. In that vein, we are urging the Energy Information Administration (EIA) of the U.S. Department of Energy to convene a “Summer Fuels Conference” to evaluate the status of gasoline, diesel and jet fuel production and inventories. We are also asking that the EIA expand the scope of its “Winter

Fuels Conference" next fall to give the agency the opportunity to share information on winter fuel production, inventories and imports with all stakeholders.

API is also eager to provide additional information on market conditions. Americans have a right to know as much as possible about this environment. Our industry is committed to working closely with the Department of Energy to monitor the situation and give Americans the latest and most accurate information available. We have participated in the Department of Energy's meetings on heating oil conditions and stand ready to provide whatever information is needed on current market conditions. API continues publishing its *Weekly Statistical Bulletin* covering production, imports, inventories and other data. Educated consumers are our best asset. We will seek to develop a joint effort with DOE to provide consumers the best and most up-to-date information available, and to help them explore ways to better cope with the fluctuation in prices.

In the short term, the government can also consider a number of actions to help prevent another recurrence of the home-heating oil situation. It can increase funding for the Low-Income Home Energy Assistance Program and more quickly and equitably release funds; and consider expanding Small Business Administration emergency loans to home heating oil dealers and truckers.

We also think it's imperative that Congress quickly reauthorize the Energy Policy and Conservation Act that provides authorization for the Strategic Petroleum Reserve and U.S. participation in the International Energy Agency.

In the long run, government can and should also take steps to strengthen our domestic oil and natural gas producing industry. Because the U.S. imports some 55 percent of the oil Americans consume, the ebbs and flows of the world oil market impact the industry's ability to continuously provide consumers the fuel they need at fully affordable prices. We can reduce rapid swings in prices by providing greater diversity in where companies get their supplies of crude oil, both at home and abroad.

We can reduce our reliance on foreign supplies and also potentially exert downward pressure on international crude oil prices by opening our most attractive domestic oil and natural gas prospects to responsible exploration and development. Currently, many of these areas have been placed off-limits by the federal government. Since 1983, access to federal lands in the western United States -- where nearly 67 percent of our onshore oil reserves and 40 percent of our natural gas reserves are located -- has declined by 60 percent. Our industry supplies the energy to keep America going strong, but to continue to produce domestic oil and natural gas, we must have improved access to federal and state lands.

Old arguments about the incompatibility of access and a clean environment have been thoroughly disproved. Technology has revolutionized how oil and natural gas are found and produced. For example, geophysicists use three-dimensional seismic equipment to locate oil and natural gas with greater precision so that more oil can be produced with fewer wells. Fewer wells mean less environmental impact. Improved drilling techniques allow companies to branch out underground to reach a variety of oil and gas reservoirs from one location. Offshore wells can now safely capture oil and gas in ocean depths of 8,000 feet in areas far offshore.

In addition to denying access for oil and gas development, the federal government has imposed layer upon layer of regulations on U.S. refineries without sufficient regard as to how these regulations impact refiners' ability to meet the full range of needs of American consumers. Refineries need flexibility to respond to the fast-paced changes in today's world. Over-regulation reduces flexibility. A soon-to-be proposed regulation to drastically lower the sulfur content of diesel fuel is an example of a government action that could have significant, negative consequences on our ability to supply heating oil and diesel fuel. We share the government's interest in further cleaning the air. But reductions beyond the 90 percent we have already proposed stand a good chance of further driving up fuel manufacturing costs unnecessarily, imposing yet additional burdens on our nation's truckers and farmers.

Even with greater access and flexibility, the United States will continue to need to rely on foreign oil supplies. Thus, it is important that we maximize the diversity of those supplies to help ensure the reliability of a continuous flow of oil imports. Unfortunately, U.S. unilateral trade sanctions and the constant threat of sanctions narrow our sources of supply, frustrating achievement of this important objective.

In recent years, unilateral economic sanctions have increasingly become the policy tool of choice in the conduct of U.S. foreign policy. One of the favorite targets of these recent sanctions has been major oil-producing countries. The U.S. currently has sanctions in place against countries comprising over 10 percent of world oil production and 16 percent of estimated remaining oil resources. With little evidence that unilateral sanctions produce desired outcomes, is there not a better way?

In short, U.S. policymakers face a dilemma. Growing supplies of crude oil will be required to sustain world economic prosperity, and diverse, ample foreign supplies are needed to help ensure our own country's economic growth. The drive to impose unilateral sanctions is an obstacle to both of these objectives.

What consumers can do

While it may be easier to see what government policymakers and the industry can do to improve the current situation, many consumers can help reduce the impact on their budgets by embracing ways to use less fuel. The industry will be doing its part to share advice for conserving fuel use in the hope that some families can benefit.

Examples of the types of changes drivers can make include: maintaining their vehicles properly, combining trips to reduce fuel consumption from cold starts of automobiles; accelerating slowly and decelerating rather than multiple braking to stop; and, in a two-car family, having the family member who does the most driving use the most fuel-efficient car. Many families will be surprised at the fuel economy benefits they can achieve from these simple changes. While they certainly won't offset the higher cost of gasoline, they should help families get where they need to go at less cost until purchasing conditions improve.

Conclusion

In closing, we share your concern for the health and welfare of your constituents. America's oil and natural gas companies have a long and proud history of providing this country's consumers with a reliable and affordable supply of energy to make their homes comfortable and take them where they need to go, when they want to go. Through good and lean years, U.S. suppliers of petroleum products have kept America's factories running and provided the fuel to move goods from manufacturers to retailer and, ultimately, into America's homes and offices.

It is because of this history of service that we understand the impact of rising prices on this nation's consumers – our customers. We are cognizant, too, of the concerns of our nation's truckers and farmers, who also have been adversely affected by these increases in fuel prices.

Finally, we recognize that you are faced with increasing demands to address this situation. To the extent to which we can help in your efforts to better understand the possible effects of the many proposed actions under consideration, we are here to assist you.

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