

SJR

308

Testimony to
Senate Resources Committee
May 5, 1986

by

Senator Joe P. Josephson

SJR 38: Federal Tax on Imported Oil

We are all familiar with the effect that OPEC has had on oil prices since 1973 and the fact that its control as a cartel has fallen apart over the past year.

There are two reasons why the OPEC cartel is now in disarray.

1. Conservation and substitution of oil by other fossil fuels and renewable sources of energy.

Arlon Tussing recently stated in the September 1985 issue of ARTA Energy Insights, "The problems of OPEC in 1982 stemmed largely from the price-induced surge in energy conservation and the severe recession. In years to come, however, the availability and price of energy supplies other than OPEC oil will cap oil-price movements. At the margin (where prices are in fact determined) coal, gas, and oil can easily substitute for one another."

2. Greater availability of non-OPEC oil.

Dr. Tussing says, "The most striking supply developments of the last five years are the small but

persistent yearly increases in non-OPEC sources. And because of declining demand, the world's reserve-to-production ratio increased 21% from 1978 to 1984."

The disarray of OPEC has caused oil prices to plummet. Instead of being overpriced, oil is now underpriced. This creates a new set of problems.

1. There is considerably less incentive to continue energy conservation measures, substitute other sources of energy for oil, or develop new oil reserves.
2. The rapid reversal in oil prices is causing severe economic problems in oil-producing states such as Alaska.

If we allow these conditions to continue, oil consumption will increase and we will offer OPEC another opportunity to force high oil prices on the world. However, it is doubtful that any price increase would be as steep as what we experienced in 1973 and 1979.

William Fisher of the University of Texas recently stated to the U.S. House of Representatives Subcommittee on Fossil and Synthetic Fuels that: "If the U.S. is to maintain the ability to produce at least two-thirds of its supply of oil and liquids, it must maintain a price sufficient for reserve replacement in the U.S. The best mechanism for such essential support is a variable import fee on imported oil and oil products."

There are five options that have been considered for taxing oil. These include:

1. Oil import tax
2. Excise tax on all crude oil
3. Motor fuels tax
4. Sales tax on energy consumption
5. Combination of oil import tariff and motor fuels tax

An April 1986 report by the Congressional Budget Office entitled The Budgetary and Economic Effects of Oil Taxes, compares each option. This report states:

"An oil import tariff would be superior to other energy taxes on this score. By raising the price of oil imports, an oil import tariff would encourage all activities that could substitute for oil imports; domestic oil production, production of substitutes for oil, conservation of oil, and substitution of other fuels for oil. It would therefore lead to the greatest possible reduction in oil imports (for a given level of tax) and provide the most assistance to domestic producers. An excise tax on foreign and domestic oil would lead to the same reduction in total oil consumption, but would burden rather than encourage domestic oil production, leading to a smaller reduction in oil imports and, therefore, putting less downward pressure on the price charged by foreign producers. A motor fuels tax would lead to a smaller reduction in oil consumption because

it would be directed at only one form of oil use and would therefore preclude many oil conservation possibilities. It would also provide no incentives for expanded domestic production. Finally, an ad valorem tax on the consumption of all fuels would lead to energy conservation, but discourage the production of domestic oil as well as all U.S. energy supply sources. These last two taxes, therefore, would do less to reduce world oil prices, encourage a reduction in oil imports, and assist the domestic oil industry."

There are always objections to a tax and the oil import tariff concept is no exception. The objections commonly voiced are:

1. The tariff will have a negative effect on the GNP.

The CBO report just cited states that: "In the short term, higher taxes of any sort could lower GNP since they reduce household income. But to the extent that taxes also reduce the federal deficit, they may tend to reduce interest rates and the international value of the dollar, which would tend to raise GNP. In view of these various offsetting influences, and the fact that the net effect of any of the taxes on nominal GNP is likely to be rather small, CBO has followed the convention that nominal GNP (not adjusted for inflation) remains approximately constant in response to a tax."

2. U.S. products will be less competitive in world markets. Again, the CBO report says: "In fact, other industrialized countries already have higher levels of oil taxes than the United States. Most of these taxes are gasoline taxes; motor fuels taxes are four to ten times higher in these countries. Taxes on other fuels also exist: Japan, for example, has an \$18.00 per barrel tax on distillate fuel while the United States has none. Higher energy taxes in these countries reflect their far greater use of sales and consumption taxes as revenue sources. Industry sources note that many of these countries appear prepared to raise their oil taxes again now that world oil prices have fallen."

3. The oil import tariff will proportionally tax the poor more than the rich. Although the CBO report states that "measured as a percent of total expenditures, the tax burden would not vary widely for families with different incomes", steps can be taken to assure that an oil import tariff does not hurt the poor. A portion of the revenues from an oil import tariff can be dedicated to programs which provide the poor with relief from energy costs, such as the weatherization program. Also, revenue can be earmarked for programs, such as revenue sharing which aid financially distressed units of local government.

In fact, non-oil producing states may favor an oil import tariff if a portion of the revenues were dedicated to revenue sharing.

The most prominent oil import tariff bill being considered by Congress is S. 1997 introduced by Senator Wallop. This bill sets a benchmark price of \$22.00 per barrel for imported oil. The tariff would apply to any oil that is priced below this benchmark. For instance if imported oil sold at \$14 a barrel, the tax would be \$8 a barrel.

An oil import tariff would:

1. Reduce the federal deficit by billions of dollars a year. A \$5 a barrel fee would generate about \$10 billion in additional revenue.
2. Increase revenue in oil producing states. An oil import tariff would be a windfall to the State of Alaska that would last as long as oil prices are depressed. If the benchmark price were \$22 a barrel, and assuming a price of \$12.50 a barrel that Standard recently posted for ANS sold on the Gulf Coast, revenues to the state could be increased by \$1.4 billion.

In conclusion, it should be said that the concept of an oil import tariff is not endorsed by the Reagan Administration and of only modest interest in Congress. One problem in establishing any level of oil tax at this

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time is that the price of oil and oil products has slipped below any logical benchmark price. Now a tax would increase prices rather than keep prices from falling farther.

Nevertheless, the State of Alaska should take a position on this issue. I believe that an oil import tariff will not only help Alaska, but also our nation, particularly if some of the revenues from the tariff are dedicated to programs which compensate those who would experience significant economic distress.

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Referred: Resources
and Finance

Dr. Jontin
File in all
legislated products
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1 IN THE SENATE

BY JOSEPHSON

2 SENATE JOINT RESOLUTION NO. 38

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 FOURTEENTH LEGISLATURE - SECOND SESSION

5 Relating to a federal tax on imported
6 oil.

7 BE IT RESOLVED BY THE LEGISLATURE OF THE STATE OF ALASKA:

8 WHEREAS rapidly fluctuating oil prices create an unstable environment
9 in Alaska and the United States for business planning and investment and
10 threaten the stability of the domestic petroleum exploration and
11 development industry, the stability of which is vital to the national
12 security; and

13 WHEREAS the continuation of energy conservation measures and further
14 development of alternative energy technologies will be jeopardized by sharp
15 declines in oil prices; and

16 WHEREAS the federal government needs additional revenue to reduce the
17 federal deficit and the threat of another period of high inflation; and

18 WHEREAS Americans face the prospect of significant budget reductions
19 in federal programs that are vital to the health, education, and welfare of
20 many Americans, but the imposition of an oil import tax would moderate the
21 severity of these reductions; and

22 WHEREAS a precipitous decline in oil prices results in major
23 reductions in revenue to oil-producing states, subjecting them to undue
24 hardships in providing the governmental services and infrastructure support
25 needed to continue the production of domestic oil at the same time that
26 these states are being given expanded responsibility as a result of
27 diminishing federal participation through revenue-sharing and similar
28 programs;

29 BE IT RESOLVED that the Alaska State Legislature encourages the United

1 States Congress to impose a federal tax on imported oil, the revenue to be
2 used to reduce the federal deficit.

3 COPIES of this resolution shall be sent to the Honorable Ronald
4 Reagan, President of the United States; the Honorable George Bush, Vice-
5 President of the United States and President of the U.S. Senate; the Honor-
6 able Thomas P. O'Neill, Jr., Speaker of the U.S. House of Representatives;
7 the Honorable Robert Dole, Majority Leader of the U.S. Senate; and to the
8 Honorable Ted Stevens and the Honorable Frank Murkowski, U.S. Senators, and
9 the Honorable Don Young, U.S. Representative, members of the Alaska delega-
10 tion in Congress.