PROPOSED ENERGY TAX LEGISLATION

HEARING

BEFORE THE

SUBCOMMITTEE ON ENERGY AND FOUNDATIONS

OF THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

NINETY-SIXTH CONGRESS

FIRST SESSION

JULY 2, 1979

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PROPOSED ENERGY TAX LEGISLATION

MONDAY, JULY 2, 1979

U.S. SENATE,
SUBCOMMITTEE ON ENERGY AND FOUNDATIONS,
COMMITTEE ON FINANCE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9 a.m. in the Crawford Room of the Natrona County Library, Hon. Malcolm Wallop presiding.

Present: Senators Wallop and Baucus.

[The press release announcing this hearing follows:]

PRESS RELEASE, JUNE 11, 1979

U.S. SENATE,
COMMITTEE ON FINANCE,
SUBCOMMITTEE ON ENERGY AND FOUNDATIONS,
Dirksen Senate Office Bldg., Washington, D.C.

SUBCOMMITTEE ON ENERGY AND FOUNDATIONS ANNOUNCES HEARING ON PROPOSED ENERGY TAX LEGISLATION

Subcommittee Chairman Mike Gravel (D-Alaska) and ranking minority member Malcolm Wallop (R-Wyo.) announced today that a hearing on proposed energy tax legislation will be held on Monday, July 2, 1979.

The hearing will begin at 9:30 A.M. in the Crawford Room, Natrona County Library, 307 East 2d St., Casper, Wyoming.

Senator Gravel stated that, "For more than six years the government has been attempting to hammer out a comprehensive national energy policy. Over the past six years this area has been the subject of a piecemeal approach. This hearing is being convened, at the request of Senators Wallop and Baucus, who serve on the Subcommittee, in an effort to secure testimony regarding our energy situation from those people in an area of the country who are not customarily able to come to Washington to present their views."

Senator Wallop added that, "It is essential that the Congress attempt to obtain the views of as many diverse interests as possible. In the past insufficient attention has been given both to those engaged in the production of oil and gas and consumers of energy in the Rocky Mountain region of the United States." He noted that he and Senator Baucus have urged the scheduling of this hearing so that people from Wyoming and Montana in particular will have an opportunity to contribute to the debate on national energy policy. "If we are to develop a national energy program which provides sufficient incentive for greater production of domestic energy and meets the needs of business and individual energy users, we must attempt to take into account the needs of individuals and businesses located in every region of this Nation," Wallop stated.

Senator Baucus has stated, "Any review of our national energy policy must begin with a review of our tax system, for it is with the use of tax incentives and penalties that we structure our energy system.

"There is no better place to conduct a review than in the West. The West supplies a high percentage of the Nation's energy needs, but incurs special problems in doing so.

"I look forward to hearing suggestions on ways to improve both the energy and tax systems."

Witnesses who desire to testify at the hearing should submit a written request to Michael Stern, Staff Director, Committee on Finance, Room 2227 Dirksen Senate Office Building, Washington, D.C. 20510, by no later than the close of business on June 22, 1979.

Legislative Reorganization Act.—Senator Gravel stated that the Legislative Reorganization Act of 1946, as amended, requires all witnesses appearing before the Committees of Congress "to file in advance written statements of their proposed testimony, and to limit their oral presentations to brief summaries of their argument."

Witnesses scheduled to testify should comply with the following rules:

(1) A copy of the statement must be filed by noon Friday, June 29, 1979, at the Office of Senator Wallop, 2201 Federal Bldg., Casper, Wyoming 82601.

(2) All witnesses must include with their written statement a summary of the principal points included in the statement.

(3) The written statements must be typed on letter-size paper (not legal size) and at least 100 copies must be submitted before the witness is scheduled to testify.

(4) Witnesses are not to read their written statements to the Subcommittee, but are to confine their oral presentations to a summary of the points included in the statement.

Written testimony.—Senator Gravel stated that the Subcommittee would be pleased to receive written testimony from those persons or organizations who wish to submit statements for the record. Statements submitted for inclusion in the record should be typewritten, not more than 25 double-spaced pages in length and mailed with five (5) copies by August 3, 1979, to Michael Stern, Staff Director, Committee on Finance, Room 2227 Dirksen Senate Office Building, Washington, D.C. 20510.

Senator WALLOP. I want to begin this morning by welcoming you, Senator Baucus. He has been gracious in agreeing to come here and help in this hearing, while we try to discover some of the effects of windfall profit tax. We are concerned with the production of energy in the Rocky Mountain area as it is related to other impediments to the easing of the Nation's energy supply situation.

I have an opening statement. Senator Baucus, would you like to make a statement?

[The opening statement of Senator Wallop follows:]

OPENING STATEMENT OF SENATOR MALCOLM WALLOP

I want to thank you all for coming here today. I see many old friends in the audience from across the state of Wyoming. It is good to be back in the State and here in Casper once again.

Before I go on I would like to introduce my good friend from Montana, Senator Baucus, who has taken a detour on his trip home to be with us today. I want to thank Senator Baucus for taking the time to come to Casper and join me in this hearing on the energy situation in the Rocky Mountain West. As a Senator, I know you have too little time to be with family and friends at home, so I greatly appreciate your joining us today, before you continue to Montana.

Senator Baucus and I are both members of the Senate Finance Committee, and together we requested a day of field hearings on the energy windfall profits tax. This is a continuation of a series of hearings that have been held on the energy problems facing the nation, and the energy tax legislation that is now before Congress. I should add a word of thanks to Senator Mike Gravel of Alaska who is the chairman of this subcommittee, but could not be with us today.

We are holding this hearing today to get the views of energy producers and consumers from the Rocky Mountain West. Wyoming, Montana, and other western states have too large a role to play in our nation's energy future for our unique problems and interests to go unheard in Congress.

There are a wide variety of energy issues that will be reviewed today, but the focus of these hearings is on issues of energy production, and the effects of the windfall profits tax on our energy situation. This focus is appropriate because of our role as an energy producing region, and because of the problems that may be created by the windfall profits tax. By focusing this hearing on the production aspects of the energy problem, I do not mean to belittle the problems facing all of us as consumers, whether we drive cars, trucks or farm vehicles. But in this energy capitol of Wyoming, a city rivaled only by Denver as the energy hub of the West, it is important for this subcommittee to look at the problems faced by producers. Our nation's leaders have failed miserably in understanding and dealing with the economic problems of energy exploration and production. Price controls, taxes and government regulations have crippled our production capacity. That my friends is why we are importing half of our energy from overseas and we now face a disgraceful and potentially disastrous energy supply situation in the United States today.

I wish that I could offer better news to you about developments in Congress, but I must admit that after the recent House passage of a punitive, vengeful energy tax bill in the House last Thursday, I am shocked and disheartened.

There are many aspects of the House tax that leave this country in an even worse position to deal with the energy situation. I am especially concerned about the reduced incentives provided for exploration and development in the early 1980's under the House plan.

So that no one is confused by the recent developments, let me compare the House tax to the one introduced by the President * * * just to give you an idea of how badly the situation has deteriorated.

The President's proposed 50 percent excise tax was increased by the Chairman of the Ways and Means Committee to 60 percent, when Congressman Ullman introduced a bill in the House.

Many people wonder what this means in terms of oil production. It means that there will be less money available to reinvest in exploration and production and ultimately, less domestically produced energy. Under the President's plan, the loss of revenues to the oil industry provides less money for investment in exploration. Based on 1978 studies of oil industry reinvestment schedules for oil exploration the windfall profits tax money would be expected to yield an additional 1.0 to 1.3 billion barrels of crude oil equivalents to proven U.S. reserves over the next three years, if industry were permitted to keep these funds. If we were to buy the same amount of oil from foreign suppliers, it would represent a balance of payments outflow of some 16 to 20 billion.

Now, let me make it clear that the tax situation has not improved in the House. By increasing the tax rate from 50 to 60 percent, the House plan would take an additional $6 billion from oil producers over the original Carter plan. The Department of Energy has estimated that the percent increase in the excise tax will retard the growth in domestic output in the early 1980's by 100,000 barrels per day over the already dismal production effects of the Carter plan!

One of the most baffling aspects of windfall profits tax is that it will not be phased out. This is a new, permanent tax on oil that has already been discovered, and oil that may be discovered in the future. What I would like to know is how the oil industry can possibly reap a windfall profit on oil that has not even been discovered yet!

There are special problems created by the windfall profits tax that are unique to the independent segment of the industry. Let me give you one example. Upon announcing the windfall profits tax, the Treasury released a table showing that without the excise tax, oil producers would net 43 cents of each additional dollar in gross revenues, and that with the windfall tax, the producer would still net 29 cents out of each additional dollar.

What the Department of Treasury forgot, or chose not to indicate is that many independent producers are not incorporated, and find themselves taxed at the 70 percent personal tax rate rather than the corporate rate used by the Treasury in its estimate. This lowers the income to producers so that even without the windfall tax, independents would net only 19 cents of each additional dollar in gross revenues. With the original windfall profits tax the independent producer would net less than 15 cents.

Another direct attack on the independents was made by denying percentage depletion on the portion of the price increase subject to the excise tax. This adds a significant negative impact on the independents' cash flow. This was not an instance of swinging to hit the major companies and accidentally hitting the independents. Percentage depletion is allowed only for the independent segment of the industry. There has been little attention given to the fact that under legislation enacted in 1976, the tax burden on independents will be increased by as much as 32 percent between 1981 and 1984.

I cannot believe that the Senate will act as irresponsibly and emotionally as the House of Representatives on this tax bill. There is a great deal of work to be done to change this proposal. For starters, I think that the Senate will have to consider adopting some kind of small producers exemption. An exclusion from the tax for the first 1,200 barrels of oil per day would shield many small independent operators from the windfall tax. I think there is more that can be done to reduce the tax burden on marginal wells and wells that produce under ten barrels per day. If we do nothing to reduce the tax burden on production from these types of wells, I fear that we will speed up the abandonment rate on wells that would otherwise produce more domestic oil.

I could continue on this morning, explaining why I oppose this so-called windfall profits tax. But I am here to get your opinions on this proposed tax, and information on how it will affect your ability to finance increased exploration and production for energy here in the Rocky Mountain West. I am interested in hearing what changes have to be made in the House bill, changes that will allow this country to get on with the job of finding and producing energy.

Senator BAUCUS. I simply want to say that I am very pleased to be here in Wyoming, because Wyoming and Montana share many of the same energy resource potentials and problems that are certainly keyed in resolving our energy crisis. There are a lot of accusations flying around the air today: Why in the world isn't the United States producing more energy? There are long lines at gas pumps in Washington, D.C. My wife and I have to alternate mornings as to who gets up at 5 o'clock in the morning to drive the cars to get gas, sit in line an hour and a half in Washington.

Here in Wyoming and also in Montana there are diesel shortages. Farmers have been able to get some diesel because of special rule No. 9 that's been amended. However, truckers can't get diesel. And they just are having terrific problems.

It's easy to blame somebody else. Government gets blamed. The Department of Energy gets blamed. Congress gets blamed. The President gets blamed. The oil companies are blamed. Ayatollah Khomeini is blamed. The Shah is blamed. Saudi Arabia is blamed. Everybody is blamed.

I think there is probably some truth in all of it. The real question is: How in the world are we in America going to begin to reestablish our position in energy self-sufficiency. I don't know that we are ever going to be independent of OPEC, whether we will ever completely cut the umbilical cord.

Nevertheless, I think we should very quickly and with immediate dispatch begin to progress as well as we can to make our country much more self-sufficient in the development of production of energy.

Of course, the key still is petroleum. We are a petroleum-based economy. We are an economy which has thrived in large part because we are a petroleum-based economy. However, that has brought us into a difficult position, because we consume so much petroleum.

We in America constitute about 5 percent of the world's population. Yet, we consume about 40 percent of the world's petroleum—a very disproportionate rate of consumption.

We also know that we can't forever and always be a petroleum-based economy in America. We are going to have to diversify, particularly if we are going to rely less upon OPEC. We are going to have to develop other sources of energy, not all oil, but some might be oil related. Some would be called synthetic fuels. Some would be the renewable sources of energy such as solar, biomass, but the point is we have to begin to develop.

And also, I think it's safe to say that as much as we want to increase petroleum production and as much as we want free enterprise and profit motive to be the base, the foundation, still there is a limit. We can't put all our eggs in a petroleum basket, because the more we do, the more we are going to postpone the day when we have to begin to diversify.

I am not saying that we should immediately close the valve, begin to put ourselves in a position where we are forced to diversify, but I'm saying we have to develop, in my judgment, policies which are aware of the need to begin diversifying in other forms of energy.

So, it's a combination. I'm hopeful this morning, this afternoon—it's my understanding we will continue straight on and not break through lunch until about 2, 2:15 or so. And then I have a plane to catch. I don't know what other plans will be after that for the rest of the participants.

It's my hope during these next few hours we can begin to get some hard solid facts, particularly to the petroleum industry, so we can determine whether or not and to what degree a severance tax, windfall profit tax, whatever you want to call it, makes any sense.

It's not a time for rhetoric. It's not a time, in my judgment, for lots of blame. It's easy to blame anybody. I think rather it's a time, as I said, get solid information so we have a very productive several hours.

In conclusion, let me say I am very honored to be here, particularly with Malcolm, a tremendous Senator. We have served together on the Finance Committee. And together we will be working, I know, toward trying to develop some kind of sanity to all this energy chaos and with your help—and it's going to take your help—to begin to put America back on the road toward self-sufficiency.

Senator WALLOP. Thank you, Senator Baucus.

I'd like to introduce to all of you and thank personally Jim Heinhold and Jack Nutter and also Bob Reynolds of my staff. Jim and Jack are on the Finance Committee staff. And they are a capable, well-informed pair of young men. They are of great assistance to me in the work that we are doing.

While I was on my way out here in the airplane, having read most of the material I brought along, I searched around and found the United Airlines magazine. In that was a piece of research summary by the Morgan Stanley Research Investment Corp., dated May 7, 1979.

It's probably a long time since anybody has read the United Airlines magazine, but they should read it. I would like to read a couple paragraphs from it.

It says:

In point of fact, the independent seems to be the forgotten man in the debate as to what constitutes adequate cash flow and incentive. The large multinational companies with diverse business interests and multiplicity of earning sources do indeed enjoy considerable financial flexibility and for the moment strong comparative earnings aided partially by a dramatic improvement in foreign downstream margins. The independent, whose sole source of income is domestic production, is clearly in a very different position. Yet, it is the independent who is still responsible for around three-quarters of the wells drilled in the United States and who is most affected by continued regulation. The Nation will not be well served if he choses to quit the business.

It goes on then to talk about the purpose of the phased decontrol. But it says:

Somewhat overlooked in the debate is the fact that the Department of Energy for nearly the past 2 years has been administering crude prices at levels considerably under the maximum provided under the Energy Policy and Conservation Act. For example, the composite price of crude was recently around $1 per barrel under the permitted ceiling. As a result, producer "deficit revenues"—revenues that could have been collected had DOE allowed maximum incentives provided under the law—are now in excess of $4 billion and accumulating at over $400 million per month. The ironic thing about this situation is that the oil producers would not be materially worse off between now and October 1981 if DOE were to restore the accumulated windfall loss, allow maximum permitted prices over the following 28 months, and then let controls expire as scheduled. This is a point liberal politicians chose to ignore in their zeal to festoon the landscape with baloney.

Then it makes a recommendation, which I think would be interesting:

We believe, therefore, that investors should concentrate on companies whose earnings gain in the immediate future are not heavily predicted on higher domestic crude prices. These would include Atlantic Richfield and Sohio, increased North Slope production, Marathon, major 1980 impact from refinery upgrading programs, all of which are in the Morgan Stanley model portfolio and Phillips, rising North Sea output.

Primarily, you should look to companies who have a source of foreign oil supply.

I thought this was rather interesting. I want to express an opinion of my own before we start. I think it's fair to point out that you can tax as much as you would like on the cost of production so long as you subscribe to the theory that we have found the last barrel of oil and the last cubic foot of gas, and are only waiting to pump it or produce it. If the country has given up, so be it; but if you think, as I do, there may yet be a future for us, then we have no choice but to take into consideration the cost of replacing those barrels and those cubic feet of gas and tax accordingly.

[The summary referred to follows:]

MORGAN STANLEY RESEARCH SUMMARY EXCERPT

OIL INDUSTRY: THE BATTLE FOR DECONTROL

Several years ago, Atlantic Richfield (62) said it could support the elimination of percentage depletion on oil and gas if market prices were allowed to prevail. Instead, of course, Congress chose both to do away with the bulk of depletion, to broaden regulations, and even to roll back the price of what was then new (now "upper tier") oil. There are many today who recall only that Arco advocated the loss of depletion. This is likely to be Mobil's legacy if the Administration or Congress should decide that phased decontrol of upper- and lower-tier oil is indeed not necessary. Last week, Mobil advocated prices on these segments of the barrel—representing around 70% of domestic production—should continue to rise only with inflation, provided that newly discovered and stripper crude receive the world price instead of the Administration's proposed $16 per barrel price in real terms. Mobil's position can hardly be expected to endear it to a large part of the oil industry, particularly the independents.

In point of fact, the independent seems to be the forgotten man in the debate as to what constitutes adequate cash flow and incentive. The large multinational companies with diverse business interests and a multiplicity of earnings sources do indeed enjoy considerable financial flexibility and for the moment strong comparative earnings aided principally by a dramatic improvement in foreign downstream margins. The independent, whose sole source of income is domestic production, is clearly in a very different position. Yet, it is the independent who is still responsible for around three-quarters of the wells drilled in the United States and who is most affected by continued regulation. The nation will not be well served if he chooses to quit the business.

The purpose of phased decontrol is obviously not simply to enrich the coffers of the oil producers but to elicit a supply response and to reduce the regulatory burden of the entitlements program. There are essentially two methods by which potential domestic supply may be increased. The first involves exploration in new areas, and it is to this that Mobil's position is aimed. Unfortunately, there is no way of measuring how much incremental production may be achieved from such efforts. Extrapolations based on historical finding rates per foot of hole drilled are highly speculative. (One might ask, for example, what price would have been required for the Baltimore Canyon to be a major oil province.) The second method involves extracting a greater amount of oil from reservoirs that have already been discovered. Enhanced recovery from existing oil in place can be accomplished by infill drilling or secondary and tertiary recovery techniques. This method is both more measurable and more promising in the short run than total reliance on exploration success. Unfortunately, most of the areas where enhanced recovery is applicable currently qualify only for lower-tier prices, and neither existing cash flow nor incentives are adequate to proceed with the necessary programs. It is to this problem that phased decontrol is directed.

Somewhat overlooked in the debate is the fact that the Department of Energy (DOE) for nearly the past two years has been administering crude prices at levels considerably under the maximum provided under the Energy Policy and Conservation Act. For example, the composite price of crude was recently around $1 per barrel under the permitted ceiling. As a result, producers' "deficit revenues"—revenues that could have been collected had DOE allowed maximum incentives provided under the law—are now in excess of $4-billion and accumulating at over $400-million per month. The ironic thing about this situation is that oil producers would not be materially worse off between now and October 1981 if DOE were to restore the accumulated "windfall loss," allow maximum permitted prices over the following 28 months, and then let controls expire as scheduled. This is a point liberal politicians choose to ignore in their zeal to festoon the landscape with baloney.

In calculating the effect of the proposed "windfall" tax on producer income, Marathon Oil arrives at the possibility that 26%-34% of increased revenues could reach the bottom line. (This is, of course, before increased exploration expense.) The base calculation is shown below.

Estimated effect of windfall tax on producers' income

	(Dollars per barrel)
Revenue increase	$1.00
Royalty	−.14
Total	.86
50% windfall tax	−.43
Total	.43
Service tax	−.05
Total	.38
4% State income tax	−.02
Total	.36
45% Federal income tax	−.16
Total	.20
Adjustment to reflect nontaxed release of lower-tier oil	+.09
Total	.29

Marathon's figures show the industry will receive a cumulative total of $6.0-billion as the net increase in oil receipts between now and 1982 ($525-million in 1979, $2.1-billion in 1980, and $3.4-billion in 1981), while taxes and royalties will rise by $9.4-billion. However, the President will enjoy wide discretionary power over domestic crude oil prices from June 1, 1979, until September 30, 1981, and he (or his successor) could alter the currently outlined decontrol schedule at any moment. While this might be regarded as an act of political spinelessness (as Senator Kennedy now views price decontrol), it is a possibility whose reality might become more apparent should OPEC again move aggressively at its June meeting.

As we have outlined recently, domestic oil stocks have been trading at around a 5% premium to their historical normal relative price/earnings ratios. This slight premium may indicate the degree to which investors have been willing to discount decontrol and would represent a risk element should it become apparent the Administration was backing away from its current stance. One of the better analytical features of the phase-in program is that it provides a visible increment to oil companies' incomes in 1980 and 1981, years in which other basic industries might find it difficult to achieve higher profits if the long-awaited recession materializes. This would not necessarily be the case if decontrol is scuttled. We believe, therefore, that investors should concentrate on companies whose earnings gains in the immediate future are not heavily predicated on higher domestic crude prices. These would include Atlantic Richfield (62) and Sohio (48)—increased North Slope production—Marathon (68)—major 1980 impact from refinery upgrading program—all of which are in the Morgan Stanley Model Portfolio, and Phillips (35)—rising North Sea output.

Senator Baucus, as he stated, and I are both members of the Finance Committee. And together we requested a day of field hearings on the energy windfall profits tax. This is a continuation of a series of hearings that have been held on the energy problems facing the Nation and the energy tax legislation that is now before Congress.

I would like to address a word of thanks to Senator Mike Gravel of Alaska, who is the chairman of this subcommittee but could not be with us today.

We are holding this hearing to get the views of energy producers and consumers from the Rocky Mountain West. Wyoming, Montana, and other Western States have too large a role to play in our Nation's energy future for our unique problems and interests to go unheard in Congress.

There are a wide variety of energy issues that will be reviewed today, but the focus of these hearings is on issues of energy production and the effects of the windfall profits tax on our energy situation.

This focus is appropriate because of our role as an energy producing region and because of the problems that may be created by the windfall profits tax. By focusing this hearing on the production aspects of the energy problem, I do not mean to belittle the problems facing all of us as consumers, whether we drive cars, trucks, or farm vehicles or try to gain interstate transport with major trucking rigs.

But in this energy capital of Wyoming, a city rivaled only by Denver as the energy hub of the West, it is important for this subcommittee to look at the problems faced by our producers.

Our Nation's leaders have failed miserably in understanding and dealing with the economic problems of energy exploration and production. Price controls, taxes and Government regulations have crippled our production capacity. That is why we are importing half of our energy from overseas and we now face a disgraceful and potentially disastrous energy supply situation in the United States today, which, as you well know, is also beginning to drive not only our economic decision but our foreign policy decision, defense decision, and many other decisions which we ought to, as leaders of the free world, be able to make without such a heavy burden of backdoor consideration.

I wish I could offer better news to you about development in Congress, but I must admit that after the recent House passage of a punitive, vengeful energy tax bill in the House last Thursday, I have to say I am shocked and disheartened.

There are many aspects of the House tax that leave this country in an even worse position to deal with the energy situation. I am especially concerned about the reduced incentives provided for exploration and development in the early 1980's under the House plan and the signal which that action projects to those who are in or might consider investing in energy-related capital projects.

I think it is worth speculating that given the antiprofit, anti-industry sentiment in the House, will anyone take Congress up on its offer to subsidize synthetic fuel products. The risk that they face may well not be worth the problems that are attended to it.

So that no one is confused by the recent developments, let me compare the House tax to the one introduced by the President, just to give you an idea of how the situation has deteriorated.

The President's proposed 50 percent excise tax was increased by the chairman of the Ways and Means Committee to 60 percent, when Congressman Ullman introduced a bill in the House. Then the House tried seriously to pass a 70-percent windfall profits tax. It finally ended with 60 percent. In the headlines of the Washington Post, it says: "The House drastically weakens the windfall profits tax."

And let's be honest. The tax has nothing to do with profits. It occurs whether or not profit exists.

Many people will wonder what this means in terms of oil production. It means there will be less money available to reinvest in exploration and production and ultimately less domestically produced energy, and greater reliance, not less, on overseas sources of energy.

Under the President's plan, the loss of revenues to the oil industry provides less money for the investment in exploration.

Based on 1978 studies of oil industry reinvestment schedules for oil exploration, the windfall profits tax money would be expected to yield an additional 1 to 1.3 billion barrels of crude oil equivalents to proven U.S. reserves over the next 3 years, if industry were permitted to keep these funds. If we were to buy the same amount of oil from foreign suppliers, it would represent a balance of payments outflow of some $20 to $25 billion annually.

Now, let me make it clear that the tax situation has not improved in the House. By increasing the tax rate from 50 to 60 percent, the House plan would take an additional $6 billion from oil producers over the President's original plan.

The DOE has estimated that the 10-percent increase in the excise tax will retard the growth in domestic output in the early 1980's by 100,000 barrels per day over the already dismal production effects of the President's plan.

One of the most baffling aspects of the windfall profits tax is that it will not be phased out. This is a new, permanent tax on oil that has already been discovered and oil that may be discovered in the future. What I would like to know is how the oil industry can possibly reap a windfall profit on oil that has not even been discovered.

There are special problems created by the windfall profits tax that are unique to the independent segment of the industry. Let me give you one example. Upon announcing the windfall profits tax, the Treasury released a table showing that without the excise tax, oil producers would net 43 cents of each additional dollar in gross revenues, and that with the windfall tax, the producer would still net 29 cents out of each additional dollar.

What the Department of Treasury forgot, or chose not to indicate, is that many independent producers are not incorporated, and find themselves taxed at the 70 percent personal tax rather than the corporate rate used by the Treasury in its estimate. This lowers the income to producers so that even without the windfall tax, independents would net only 19 cents of each additional dollar in gross revenues. With the original windfall profits tax, the independent producer would net less than 15 cents.

Another direct attack on the independents was made by denying percentage depletion on the portion of the price increase subject to the excise tax. This adds a significant negative impact on the independents' cash flow. This was not an instance of swinging to hit the major companies and accidentally hitting the independents. Percentage depletion is allowed only for the independent segment of the industry. There has been little attention given to the fact that under legislation enacted in 1976, the tax burden on independents will be increased by as much as 32 percent between 1981 and 1984.

I have already introduced legislation along with Senator Tower of Texas that would arrest the scheduled decline in the percentage depletion rate that is to go into effect in 1980. The direction of that depends in large measure on where these windfall profits taxes go.

I cannot believe that the Senate will act as irresponsibly and emotionally as the House of Representatives on this tax bill. Interestingly enough, they voted on that without a rollcall vote. They made all their amendments. Then it was just accepted.

There is a great deal of work to be done for us to change this proposal. Senator Baucus and I along with other members of the committee will have a hard job in what is a responsible area to accomplish what is needed.

For starters, I think that the Senate will have to consider adopting some kind of small producers exemption, if we go the way of the windfall profits tax as it came from the House.

An exclusion of tax, say, for the first 1,200 barrels of oil per day would shield many small independent operators from the windfall tax. I think there is more that can be done to reduce the tax burden on marginal wells and wells that produce under 10 barrels per day. If we do nothing to reduce the tax burden on production from these types of wells, I fear that we will accelerate the abandonment rate on wells that would otherwise produce more domestic oil.

Again, make no mistake, the tax is not on the companies but on the consumers. And America shoud know it is about to start paying a $29-billion tax.

But, like Senator Baucus, I am here to get your opinions on the proposed tax and to gain more information on how it will affect your ability to finance increased exploration and production for energy here in the Rocky Mountain West and as well, the other impediments I mentioned earlier.

I am interested in hearing what changes have to be made in the House bill, changes that will allow this country to get on with the job of finding and producing energy that will free our country from the incredible burden that it suffers under right now, the world's stage, by our total dependence on the whim of people who have no interest in democracy.

With that, I have other papers that we will put into the hearing record later, but we are interested in beginning with the first panel, which is Mr. Terry Martin, executive director of the Petroleum Association of Wyoming; Thomas F. Keating from the Montana Petroleum Association; and Mr. Stan Sprinkle, Independent Petroleum Association of the Mountain States.

Gentlemen, you may proceed in any manner you would like.

STATEMENT OF TERRY MARTIN, EXECUTIVE DIRECTOR, PETROLEUM ASSOCIATION OF WYOMING

Mr. MARTIN. Mr. Chairman, members of the subcommittee, my name is Robert H. Martin. I am executive director of the Petroleum Association of Wyoming, a division of the Rocky Mountain Oil & Gas Association. My office and my home are here in Casper. I appear here today in behalf of the nearly 800 members of the region's oldest and most respected oil industry trade association, members who produce 95 percent of the crude oil in Wyoming.

I have been employed by RMOGA for nearly 25 years and have been an interested observer and active participant in industry affairs since the end of the Korean conflict, through the Vietnam war, and 2½ years of President Carter's moral equivalent war.

I have frequently seen the industry's fortunes rise and fall as the supply-and-demand equation changed to reflect the needs of the country for plentiful supplies of petroleum-based fuel supplies. But never in those 25 years have I seen the industry so confused, so frustrated, and as a consequence so unable to perform as it is at the present time.

It is abundantly obvious that the United States is desperately in need of additional supplies of domestic crude oil and that those supplies can only be found and produced by an active and healthy industry already in place.

More than 15 years ago, ROMGA an its sister industry trade associations spent a great deal of time and effort attempting to convince the Congress of the United States, its people, and its regulatory bodies, that as the demand for crude oil in the country grew, domestic supplies would be unable to keep pace unless and until the Government recognize that identical fact, that only with a healthy, active domestic industry could we prevent the very catastrophe that we now face. To point out that our efforts fell on deaf ears would be redundant.

Even the shock of the 1973 embargo by the OPEC nations failed to alert the country to the facts of life, but in retrospect, seemed to stampede our lawmakers and administrators into a frenzy of statutory and regulatory mistakes that have subsequently robbed the oil and gas industry of the momentum and vitality need to keep up with the demands on crue oil supplies.

While we applaud the fact that President Carter finally announced his intention to begin removing controls from domestic oil prices, his insistence that Congress also impose a crushing tax on oil industry revenues creates a clearly counterproductive atmosphere that can only lead to a worsening of the current crisis.

Decontrol, as we see it, was not proposed to benefit the oil industry, but to increase the Nation's domestic energy resources and reduce dependence on imported crude oil supplies. Unfortunately, the Congress seems to have lost sight of that purpose and has instead become preoccupied with the matter of so-called excess or windfall profits, forgetting that the domestic producing industry has been operating under regulatory constraints which have seriously reduced profits.

Indeed, if the question is who will benefit from decontrol and tax legislation now under consideration by Congress, the answer must be that it will be the State and Federal Governments. If a crude oil tax proposal such as the one passed last week by the House of Representatives were enacted, Government's share of revenues would probably be more than 75 percent of the additional revenues in taxes and royalties.

It seems to us that siphoning off these funds flies in the face of what decontrol is supposed to accomplish. Profits do not cause inflation but they can be a major force in reducing inflation and are an absolute essential to the business of searching for and producing additional supplies of domestic crude.

The domestic oil producers industry has been laboring under artificial price restrictions far too long. During all that time, everything we had to sell, sold at a regulated price while everything we had to buy was purchased at an ever increasing inflated price. No wonder the effort to try to find new supplies has failed to keep pace with increased demand.

Mr. Chairman, the industry in Wyoming is doing all it possibly can to find new oil, but our efforts are severely hampered. We only have 150 drilling rigs available and they are constantly in use. Wells that used to cost $200,000, now cost $300,000. Costs of services necessary to the drilling programs have risen steadily; supplies and equipment costs are literally out of sight. Labor costs are becoming onerous and it is more and more difficult to acquire and keep good crews.

There are those who constantly demand that more and more of the public lands in Wyoming and other Western States be withdrawn from exploration. There are those who would make it nearly impossible for us to move crude oil and natural gas from producing wells to market.

And the slowdown in wildcat drilling is becoming more and more evident. By the end of March this year, we had logged 17 more wildcat wells than for the same period in 1978, 103 to 86. The last figures available for the second quarter of 1979, the week ending June 22, show the margin was down to four wildcats, 181 in 1978 to 177 this year.

If that progression holds true for the last week of June 1979, it will mean that wildcat drilling is on the downgrade and therefore the possibility of finding new reserves has been seriously depressed.

In closing, let me say that we have watched with trepidation the past 2 years the actions of the Congress and those administrative agencies having regulatory control over our industry. The scene seems to us to change almost daily as regulatory agencies overreact to current events and consequently overcontrol.

But, Mr. Chairman, nothing we have seen during the past 2 years, nothing done either by Congress or the regulatory agencies, has helped produce one more barrel of crude oil. And now we find the Congress so preoccupied with imposing new taxes that we are afraid it will miss its last opportunity to provide the industry with the push it really needs to move the country closer to plentiful supplies of crude oil and the products produced therefrom.

Mr. Chairman, we plead for your understanding and express our hope that these conversations will help you understand our problem. We thank you for your courtesy today and for the opportunity to comment.

Senator WALLOP. Thank you.

STATEMENT OF STAN SPRINKLE, CHAIRMAN, INDEPENDENT PETROLEUM ASSOCIATION OF THE MOUNTAIN STATES TAX COMMITTEE

Mr. SPRINKLE. Mr. Chairman, members of the subcommittee, I am Stan Sprinkle, chairman of the Independent Petroleum Association of the Mountain States Tax Committee. I have been asked to be here today to make this presentation on behalf of IPAMS. By occupation, I am a CPA and tax partner with Peat, Marwick, Mitchell & Co.

IPAMS represents 11 States in the Rocky Mountain region with over 1,000 members. Therefore, we appreciate this opportunity to make these remarks today.

On April 26, 1979, President Carter released his detailed specifications——

[Discussion off the record.]

Mr. SPRINKLE. As I indicated, on April 26, 1979, President Carter released his detailed specifications of the windfall profits tax which is intended to accompany his plan for phased decontrol of domestic crude oil prices. Since that date, members of IPAMS have been very active trying to inform the public and their Congressmen and Senators as to why the tax would be a significant burden on the domestic oil and gas industry.

On May 1, 1979, IPAMS adopted a resolution opposing the proposed windfall profits tax on the grounds that such a tax would, one, reduce or eliminate the incentives brought about by decontrol to increase domestic crude oil production; two, provide no price relief to the average consumer who is dependent upon crude oil products; three, diminish the ability of domestic producers to explore for and develop the vast undiscovered oil and gas resources of the United States; and four, extend a philosophy of Government involvement in private industry that is adverse to the basic tenets of a free and open society.

The proposed windfall profits tax will be a permanent 50 percent excise tax, becoming effective on January 1, 1980, imposed at the wellhead on the owners of domestic crude oil, that is, producers and royalty owners. Oil selling at uncontrolled prices including stripper well oil, newly discovered oil and incremental new production from tertiary recovery projects would be taxed.

It is clear to the oil industry that characterization of the President's proposal as a windfall profits tax is totally inaccurate and grossly misleading. First, it is not a windfall profits tax but rather an excise tax payable regardless of whether there are profits. Second, under existing tax laws, more than half of each additional $1 earned from phased decontrol would already go to the county, State and Federal Government. Thus, the chief recipient of any windfall from increased prices already will be Government; not the oil producers.

The White House has said that under the proposed tax structure, producers would be able to keep 29 cents out of each extra $1 generated by the decontrol program. This compares with 43 cents without the excise tax. However, the retention by the independent producers will probably be less that 20 cents out of each extra $1 generated.

Since a windfall profits tax would divert badly needed funds from the industry at a time when substantial amounts of capital is needed for exploration, many congressional leaders and industry people have advocated a windfall profits tax coupled with a plowback. The theory of plowback has considerable merit, but from a practical standpoint, is next to impossible to design without flaws affecting large segments of the oil industry.

One of the main problems with a plowback is that the President's proposal requires the tax to be collected before a producer could earn the plowback credit. Since the Treasury Department would have collected the tax in advance, the funds to make a plowback would not be available. Therefore, the producer, in most cases, would have to borrow funds in order to earn the credit. However, borrowing funds for wildcat drilling and other high-risk expenditures may not be possible. And most producers would be cautious in borrowing such funds.

Another problem with a plowback is that in prior versions of a plowback, and most likely with this one, a producer would have to exceed a plowback threshold. This creates many problems due to the different levels of operation of different producers and even of a particular producer from one year to another.

For example, a producer who, during the base period, had a very active drilling program would have a very high threshold which could easily result in expenditures being well in excess of cash flow. To the contrary, a producer who, during the base period, had a low ratio of expenditures to income, would have a much lower threshold of required expenditures.

Application of plowback proposals to actual operating case histories indicates that, in many instances, the active producer that has been active in the exploration area will exhaust his cash flow before reaching his threshold investment level and therefore will be unable to qualify for credit. Many producers must have the cash from the plowback credits in hand to be able to earn the credits in the first place.

If a windfall profits tax must be enacted in order to assure the continuation of a phased decontrol, then a plowback provision must have a reasonable threshold level and the tax must not be levied until after the producer does not make the required qualified expenditures. Than and only then will the industry have the funds, risk capital, which are required to meet the challenges of the future.

In summary, decontrol without a windfall tax, with or without a plowback provision, is the best way to provide an economic atmosphere which is critical if the oil producer is to continue to expend substantial amounts of risk capital in looking for new crude oil reserves. There can be little question that decontrol is essential for the future economic health of the United States.

I wish to thank you for this opportunity.

[The attachment to Mr. Sprinkle's statement follows:]

SUMMARY OF CRUDE OIL PRICE DECONTROL AND PROPOSED WINDFALL PROFITS TAX

Oil categories	Price decontrol mechanism	Amount subject to windfall tax [2]	Volume subject to windfall Tax [2]
Decontrolled crude oil, stripper well crude oil, sacremental tertiary naval petroleum reserve, newly discovered oil effective June 1, 1979).	Uncontrolled	Difference between world price and market incentive tier base price.[3]	All oil not otherwise subject to tax as lower tier or upper tier taxable volume, excluding ANS oil and Federal royalties.
Upper tier oil	Commencing Jan. 1, 1980 upper tier ceiling price will increase in equal monthly increments to world price by Oct. 1, 1981.	Difference between the sale price as the upper tier price is decontrolled [1] and the constructive upper tier controlled base price.[4]	All upper tier oil except oil otherwise subject to tax at lower tier level.
Lower tier oil	Lower tier oil to be phased out through reduction in base production control level (BPCL); BPCL reduced 1½ percent per month from Jan. 1, 1979 through Dec. 31, 1979 (effective June 1, 1979 with a one-time 9 percent reduction in the BPCL); 3 percent per month from Jan. 1, 1980 through Sept. 30, 1981; decontrolled effective Oct. 1, 1981.	do	Volume of lower tier oil freed to the upper tier price not in excess of the amount released if the BPCL was reduced by 2 percent per month commencing Jan. 1, 1980.
		Difference between the sales price as the upper tier price is decontrolled [1] and the lower tier price (or constructive lower tier controlled base price [5] after Sept. 30, 1981).	Volume of lower tier oil freed to the upper tier price in excess of the amount released if the BPCL was reduced by 2 percent per month commencing Jan. 1, 1980.
		None	Volume of lower tier oil at or below declining BPCL is not subject to windfall tax.
Marginal production	Upper tier price for sales in excess of 20 percent of base level determined using 1978 lower tier oil effective June 1, 1979 through Dec. 31, 1979; upper tier price for all sales beginning Jan. 1, 1980.	Difference between the sales price as the upper tier price is decontrolled [1] and the constructive upper tier controlled base price.[4]	All marginal production subsequent to Jan. 1, 1980 is included in the upper tier volume.
Financed recovery, lower tier oil released to upper tier.	Specified volumes of lower tier oil released to the upper tier price to finance investment in enhanced recovery projects commencing Jan. 1, 1980. (Final rule has not been issued by DOE).	do	Sales at upper tier prices included in upper tier volume.
(Alaskan North Slope oil ANS).	Uncontrolled	None	None.
Royalties—Federal Government.	Various—depends on category of crude oil produced.	do	Do.

[1] Technically after Sept. 30, 1981, reference to the upper tier price will no longer apply; at that time it will be the uncontrolled, receiving market sharing or world price.

[2] The rate of 50 percent is applied to product of (taxable amount subject to windfall profits tax) × (volume subject to windfall profits tax), effective Jan. 1, 1980. Any amount subject to the windfall profits tax is to be excluded from the definition of gross income for purposes of computing percentage depletion.

[3] Market Incentive Tier Base Price is designated at $16 per barrel for the quarter ending December 1979; adjusted quarterly for inflation.

[4] Constructive upper tier controlled base price is the price at which upper tier would have been controlled if the DOE decontrol mechanism had not been implemented. The constructive upper tier controlled base price will be increased over a 50-month period to the market incentive tier base price by January 1980.

[5] Constructive lower tier controlled base price is price at which lower tier would have been controlled if DOE control had not been implemented. The lower tier controlled base price will become meaningless in May 1983 when the lower tier taxable volume becomes zero.

Senator WALLOP. Thank you.

STATEMENT OF THOMAS F. KEATING, MONTANA PETROLEUM ASSOCIATION

Mr. KEATING. My name is Thomas F. Keating. I am from Billings, Mont. I am representing the Montana Petroleum Association, the Montana Association of Petroleum Land. I am also a member of the Independent Petroleum Association of America and the American Association of Petroleum Landmen. I operate a leasing land service in Montana. I am president of Cherry Creek Oil Co. as an independent operator.

The topic for the hearing this morning is windfall profits tax as proposed by our President. To begin with, I object to the title of the proposal. As you have heard, this tax has absolutely nothing to do with profits. Most of all, the reason I object to the title is that it is misleading to the American public. It has created great misunderstanding and tremendous anamosity at a time when this country should be pulling together as a people with a single objective of improving our economy.

There is misunderstanding and panic among the various factions and groups, all of which is caused by the misleading information from Washington, D.C., through the media of this country. This misinformation creates unnecessary suspicion which interferes with the normal operations.

In my business as a landman, I am in contact with people in the general public from all walks of life, from farmers and ranchers to doctors and lawyers and business people on the street. The confusion over the energy crisis is unbelievable. And there is really no reason for it.

This industry needs capital to operate and capital is generated by profit. To label profit as a "sin" is to deny this industry of the means for operation. Actual decontrol of the price of oil as proposed would be beneficial to this industry and to the people of this country.

It has been demonstrated historically that the profits from the oil industry are constantly plowed back into more exploration for the purpose of finding more oil. It is also clearly demonstrated that the more exploration, the more production is found. If we are truly to increase, we must have an incentive. And that incentive must be total decontrol of our industry.

The increased price in oil without the tax will eventually go back to the American people through all of the expenditures in the industry. Profits produce capital for exploration. Profits also produce income for stockholders. Profits also create jobs for workers. Profits pay for supplies, which in turn create jobs.

In a word, a profitable economy is a healthy economy. An economy that is overtaxed is unhealthy.

The current U.S. reserves are estimated at 23 billion barrels of oil or gas equivalent. In the last 5 years, Mexico has been exploring in its own country and has developed 700 billion barrels of new oil in reserves. That's about 35 times more than the United States has in reserves now.

To say that there is no new oil or that oil can't be found is erroneous. There are large areas of the Western United States that are virtually unexplored and have the potential of great reserves which will make us less dependent on foreign sources of oil.

This exploration is extremely expensive. It can only be discovered if there are profits from production to be reinvested in exploration.

We need, first of all, an increase in price without taxation. And we need a reduction of Federal interference, such as moratoriums on leasing, expansion of wilderness areas, archeological siting requirements and environmental impact studies, all of which interfere with development and exploration.

Our industry is doing the best it can in finding new oil and developing secondary tertiary oil reserves, all of which cost money. Our profits are up an average of 57 percent. And by comparison with other industries, we are laggards.

The average increase in profits in the paper company, for paper industry in the last 6 months, is 100 percent increase. The railroads have increased their profits by 190 percent. Nonferrous metal industry has increased its profits by 350 percent. The steel industry has increased their profits by 4,282 percent.

Our rate of return on investment in the oil industry in the past 20 years has been at the rate of 10.8 percent. All other industries have a return on investment of 11.4 percent.

Senator BAUCUS. What did you say the return is for oil and gas industry?

Mr. KEATING. For the last 20 years in the oil and gas industry, the rate of return has been 10.8 percent.

Senator BAUCUS. What has it been in the last 10, if you know?

Mr. KEATING. The return on investment in 1977 was 14.6 percent for the oil industry and 15.2 percent for all other manufacturing companies. Off the top of my head, in the last 5 years, the oil industry has been slightly lower than all manufacturing combined. That's the rate of return on investment.

The percentage of profits has also been less. And again, I'm speaking from memory. The rate of profit for the 30 major companies in 1978 was roughly 4.2 percent. And for all other industries, it was 5.8 percent. That was for 1978.

These are documents by the Chase-Manhattan Bank study.

As an example of profits being beneficial to the consumer, I would like to point out to the computer calculator industry, 5 years ago, most small firms could not afford a computer and most individuals could not afford a calculator. The profits of that industry through their increased technology were phenomenal. And in fact, the stock of various corporations in this industry were meteoric in their rise. And now after 5 or 6 years of keen competition in unrestricted regulations most small firms can afford a computer if they need one and almost everybody, including many housewives are carrying calculators with them to the grocery stores, all because the supply has increased to meet the demand and the competitive nature of the business has driven the price down so anyone can afford it.

I cite this example to say that I am sure that the oil industry will do the same thing, since within itself it is highly competitive. And if we are allowed to explore for oil and gas with the profits we rightfully earned and deserve, we will increase the supply to meet the demand in this country and thereby reduce the price to the consumer so that he will be getting a fair product for a fair price.

Our Republic was founded on the capitalist system. This industry epitomizes the capitalist free enterprise system. The products from this industry touch every citizen of the United States. The products from this industry make up a large portion of the commodities consumed by the citizens of the United States.

If the Congress of the United States is to promote the general welfare of the citizens, I would say that if you would promote the general welfare of the oil industry, you would be doing a service to the citizens of the United States.

Thank you very much for letting me be here.

Senator WALLOP. Thank you. Thank you all for your testimony.

Let me begin with Mr. Sprinkle. As an accountant, is there a rollback on tertiary recovery process contemplated under the windfall profits tax as it's drafted? Does it in effect amount to a rollback? Anyone at the table can answer the question.

I'm not talking about plowback. I'm talking about the price you could get under the existing law, the return you could get under the existing proposed versus what would happen with the tax proposals that go to tertiary recovery.

Mr. SPRINKLE. I am not real sure, but as I recall, in a way the tertiary process is subjected to the windfall profits tax. And therefore, in effect, there really is a rollback on price, just as the stripper wells presently—they have been decontrolled right along. And now it's subjected to the windfall tax. In effect, there is a rollback. I believe tertiary is the same way, incremental tertiary.

Senator WALLOP. Let me ask you three gentlemen, we hear plowback discussions in Washington, but I contemplated and I wonder if with plowback provision you don't discourage outside risk capital that would otherwise be coming in.

Someone with an interest or someone who made it big with Pizza Hut for instance, had some money he wanted to invest. Is there an incentive to putting it into something that he can't get it back out of, where it has to continually stay there or risk totally punitive taxes at the end of time when he wants to get out of the investment?

Mr. SPRINKLE. I don't think there is any question that the risk capital is very hard to raise by the independent. And a lot of the capital that is raised is not from within the industry itself. It is, as you indicated, from other outside sources.

Without a plowback, I would suppose, yes, there will be a problem of raising that risk capital. However, I think with pure decontrol without any plowback or taxes in effect—I mean, without any tax is the best way to go. I would be glad to leave you some charts here, but one of the charts has been assembled by the Independent Petroleum Association of America. And this is based upon information from the U.S. Bureau of the Census for the years 1973 through 1977. The value of production at the wellhead during that time period was $33.3 billion.

Also, during that 5-year time period, expenditures for drilling and development costs and production costs totalled $34.9, which is a big 1.6 more in expenditures than the value of the product at the wellhead. So, already the independent segment is plowing back the revenue.

Now, I failed to mention that this excludes the top 24 largest companies, producers. And this is based on information from the U.S. Census Bureau.

So, you take that 5-year period from 1973 through 1977, they are already plowing back or spending more money than the gross value of production at the wellhead. So, I think if you have decontrol without tax, you are going to find that you have a lot more money going back into the ground than with any type of tax.

Senator WALLOP. I guess my question is directed more toward knowing the kinds of effects plowback has on the people who are in the business.

Mr. MARTIN. I think one of your subsequent panels—some of the witnesses may express themselves on this very thing.

Senator BAUCUS. Who would they be?

Mr. MARTIN. Mr. Morton and some of the others.

Mr. KEATING. I would like to comment that I think a plowback provision from Congress would be redundant. We are already plowing back our profits and borrowing more money, outside money, all the time. The disincentive to outside money is the threat against the elimination of the depression allowance, the attack on the taxation advantages, the attacks on intangible drilling costs, and the other various tax proposals that are really anti-investment and anti-industry.

Senator WALLOP. I will pursue that with the others, because I think it has to do with the investment structure that takes place, anyway.

Mr. William Smith, who is the president of Champlin Petroleum, testified on behalf of the API, stated before the Ways and Means Committee recently that a substantial amount of oil and natural gas can still be found in this country, perhaps 40 times the current annual production. Would you gentlemen agree with that assessment?

Mr. MARTIN. Certainly.

Mr. KEATING. If we are given the room to explore, I am sure it will be found.

Senator BAUCUS. What additional domestic production——

Mr. KEATING. The cost of finding oil now is roughly $9 to $10 a barrel on a known reserve factor, but the risk is higher now because the known areas—the easy areas have been exploited.

What we are looking at are really wildcats that need more study. And so we are going to be expending a greater percentage of the price of the oil.

Senator BAUCUS. I am wondering what associations or organizations from the industry have worked up figures that show additional barrels of oil that will be discovered and produced in America as domestic production, at what levels of price. Say $9 or $10 roughly. Would it be $12? Would it be $15, $20, $25? I assume that the figure 40 times the present, that we can find a lot more oil, assumes probably a pretty high price to go down and to drill—I don't know—20,000 feet or something.

Mr. MARTIN. I don't think there can be a common denominator in the sense of price. We do have some figures we developed recently for the overthrust area, for the potential for new reserves. I think when you try to equate that into a standard or common denominator, the price per barrel, how much each price would encourage for development, I don't think you can arrive there. Each well drilled is a separate entity itself.

I think you just run out at the end of the string very quickly if you try to do that.

Senator BAUCUS. What do you mean?

Mr. MARTIN. Each operation, each drilling program, is quite different as to depth, as to the area they are drilling, the area, the kind of well it is, the kind of acquisition costs, and the lands and one thing and another. So, to try to develop a common denominator as to price—would $10 oil have created five wells or did it create one well, would $20 crude oil—I don't think you could speculate.

Senator WALLOP. You can speculate on what it would do to already discovered oil?

Mr. MARTIN. Yes.

Senator WALLOP. As the price goes up on that, the more attractive it becomes to try to draw the last drop out.

Senator BAUCUS. Some wells are more expensive to drill than some others?

Mr. MARTIN. Naturally.

Senator WALLOP. I might point out that as the price goes up, the more tertiary projects would be done because it would be economic to try to get some of that oil. That's discovered crude. And it's somewhat different.

Senator BAUCUS. Thank you.

Mr. SPRINKLE. I think if you go back and look at the last 5, 10 years, you will find a correlation with price, drilling activity, new reserves, that price has been going up. There has been more drilling, more new wildcat drilling done, more new wells discovered, but as far as trying to correlate, you know, that you need $10 or $20 oil——

Senator BAUCUS. I agree it's very speculative. I was trying to get some handles here.

Mr. KEATING. The Chase-Manhattan Bank did a study. And they estimated that in the next 5 years, it would take $350 billion for the necessary exploration to increase our reserves, to reduce our imports by about 10 or 15 percent.

Senator WALLOP. That's $350 billion?

Mr. KEATING. $350 billion. And the industry is generating about $100 million. So, we need outside money or we need to generate a lot more money from the industry. And that would be naturally through a price increase without taxes.

Senator WALLOP. Terry, could you comment on the availability of drilling rigs in the area? And do you anticipate shortages?

Mr. MARTIN. Senator Wallop, my only comment was, it seems to me looking at the number of rigs active in Wyoming at any given time, the maximum for the last couple years has been 150. They are being built as fast as they can be built.

In the yards right here in Casper, I have noticed in the last 2 months two or three new drilling rigs. They are machines. They need rest once in awhile. They have to be moved once in awhile. It's a pretty expensive business to get into. We need all we can get.

Senator WALLOP. Is there a shortage now?

Mr. MARTIN. A shortage to the extent there are more applications to drill wells than there are rigs to drill them.

Senator WALLOP. How long a time—I suppose that depends on where it is. How long do you have to wait?

Mr. MARTIN. Years. The wells are much deeper now and the rig is on the location longer for each well. They are not quite as mobile as they used to be.

Senator WALLOP. In the House-passed version of the oil tax as a general tax rate, as I mentioned, of 60 percent, there is a so-called special tax rate of 50 percent on newly discovered oil when the price of it is between $17 and $26. The House Ways and Means Committee described that 50 percent as an incentive for newly discovered oil. I wonder if you gentlemen would characterize 50 percent tax as an incentive?

Mr. MARTIN. It's a little difficult for me to swallow.

Mr. KEATING. One thing we should comment on is the fact that the U.S. Government is the largest single royalty owner at the present time. And if the price of oil goes up, the royalty is going to go up correspondingly. And the same thing with the State. The State of Wyoming and the State of Montana have ad valorem taxes based on a percentage of the value of the oil.

So, if the price of a barrel of oil goes up in Montana, then the value to the State increases correspondingly.

Senator BAUCUS. What is that rate for Montana and Wyoming?

Mr. KEATING. It varies from county to county. It varies from 10 percent to 18 percent, depending on the county.

Mr. MARTIN. Our property taxes in Wyoming are in excess of 6½ percent. And our severance tax is 4 percent at the current time. Our crude oil is valued at 100 percent, not at any fraction thereof. As a consequence, Wyoming producers probably pay more per barrel in taxes than some of the surrounding States because of the difference in the formula.

Property taxes may reach as high as 7 percent this year. The initial figures are about ready. So, that would rush in up—it amounts to 11 percent which is not deductible under the windfall profits tax bill.

Senator BAUCUS. I thought it was.

Mr. MARTIN. Again, we have not seen the bill that was passed, but in all the reports I read—and I just read a report on the President's bill, in which it says it is not deductible.

We have some confusion in Wyoming, wondering what the value of crude oil will be for State tax purposes right now under the sort of tax that legislation is considering. Whether 50 percent tax would be deducted from the value for tax purposes in Wyoming or not, we still don't know and probably won't for a while.

Senator WALLOP. One of the things that troubles me about the House-passed bill is that on a given barrel of oil—at least some of the older barrels of oil, there are separate taxes that have to be computed for each portion of it. And then they have to be paid twice a month.

What would happen, if some kind of windfall profits tax is necessary, if we made that collectible annually rather than bimonthly? Would that help the cash flow situation?

Mr. MARTIN. Certainly.

Mr. SPRINKLE. I think without question that would help the cash flow situation when you start looking at plowback provisions. However, what you are talking about is your taxes on domestic production. And that becomes a very small percentage of the total crude used in this country when you look at the imports.

Senator WALLOP. That's one of the interesting effects of this. I don't think the public has realized that the majors with the large overseas reserves or access and all of that is not subject to windfall profits taxes. The tax simply makes it more attractive to broker that oil between producers and consumers.

They really act as bankers, do they not, in the major oil companies' activities overseas? And that makes that oil industry more attractive to the extent you can find it, but find it on the world market?

Mr. SPRINKLE. With the uncertainty today as to where a windfall profits tax may be or where it's going to end up on, I can tell you from a personal situation—a client situation, actually, in Denver had developed acreage in Wyoming. He has been in the business for 30 years. He cited that he did not know where their risk capital was going to come from in order to explore that acreage. They decided as group shareholders that they would see about selling their reserves versus staying in business.

They have just contemplated—I mean, just approved a plan to be acquired by a major oil company at this point.

But with the severity of raising capital right now, the risk capital for drilling, I think we are going to see more and more of this. So, we are going to be seeing more constraints involved in the future in the way of production and fewer companies, because it has become so expensive to drill, particularly in the western part of the States where a lot of areas haven't been explored at this point. It's very expensive to drill in this area.

And as to where that capital is going to come from, it's hard to find it. So, we are going to see, I think, more and more companies being acquired by the majors all the time.

Senator BAUCUS. I understand your point and I agree with you, but in some sense, aren't we a little bit in a vicious circle here, because the more the price of energy rises, the greater the rising capital costs are. And it's kind of a neverending circle to a degree. Part of the reason drilling costs have increased is because of energy costs. And steel is more expensive.

As one example, I read an article in the Wall Street Journal. The effect of the article was the majors aren't at all upset about this windfall profits tax, because it falls very heavily on the independents.

Would any of you like to comment on this? Is there a disparity in the President's proposal, 50 percent, between how it falls upon the majors and independents? Any of you?

Mr. KEATING. The most obvious point is that the major oil companies are international in scope. And a portion of their profits is derived from their overseas business, where as the independent derives 100 percent of his income domestically.

So that the domestic tax effects 100 percent of the independent and maybe not 100 percent of the major oil companies.

But I would be opposed to this type of comparison. I would hope to see divisiveness in our industry.

The majors have a place in this industry and so does the independent. And I don't want to get into an argument between the independents and the majors. I do not want to see our industry divided in our objective of finding oil.

There are areas where largeness is a necessity for exploration. And there are other areas where the independent can do his job.

We talk about the rising price of goods and services. The oil industry or the independent has been restricted in his income by the ceiling on oil, whereas other prices are not restricted. Now, the value of the dollar is decreased. The price of oil has not gone up necessarily. We are paying more dollars for services and supplies, and receiving the same number of dollars for our oil that we are producing now. And the value of that dollar is decreasing.

So, as we are regulated, our oil becomes worth less.

Senator BAUCUS. Aren't most independents in different tax brackets? Aren't they taxed much more heavily than the corporate, because the corporate, maximum corporate, rate is lower than the maximum independent rate?

Mr. KEATING. Depends on whether the independent is incorporated or operating as an individual.

Senator BAUCUS. Isn't it true that the corporate tends to be taxed less than the independent?

Mr. KEATING. I don't think so. I think as of lately, everybody is incorporated. In fact, it's wise for an independent to incorporate at the present time.

Senator WALLOP. I don't think the object is to try to drive a wedge between the industry. I think the effect of it is different, depending on how your corporate industry is. If you are operating with a high percentage of overseas petroleum products that are not subject to tax and you have a fairly substantial internal capitalization, you are not going to have the same cash flow problems that an independent producer is going to have who has to pay a tax twice a month.

Mr. KEATING. I still see those proposals and regulations as a regulation on business or regulation on profits.

I will ask why in our free enterprise system does there have to be a regulation on price of a single industry or on our profits, for that matter? It is advantageous to the consumer if we are allowed to make a profit because of the number of consumers that are in our industry, the number of consumers that have invested in our industry, the number of consumers that benefit by the products that we can supply them at a fair price.

What is a hindrance in this is the amount of money that the Federal Government is taking off the top from both the citizens and the operators to use in other ways.

Senator BAUCUS. It would be helpful for me if you could break down where—let's assume complete decontrol in the next couple years. Let's assume the President's approach to windfall profits—if you could break down where every penny goes to the degree that you can: that is, how much is going to be Uncle Sam's? How much is going to go to Wyoming or counties? How much is going to go to the independent? How much is going to go where?

Is it possible at all to work that up for the record?

Mr. KEATING. It could be worked up, but why?

Senator BAUCUS. The reason why is because the information I have that is worked up by the Joint Committee on Taxation—the joint House-Senate committee staff—is that the President's bill amounts to on the average between now and 1984 approximately 30 percent, lower than 30 percent effective tax rate on the gain.

You said that independents get about 19 cents or less than 20 cents on the dollar. And that doesn't square with what I get, at least, on the surface. That's why I have asked the question. Because I am trying to get to the bottom of this and find out what is the actual effect to the independent and to other parties that are involved in all this.

Mr. SPRINKLE. There may be some of the others that may have some sort of breakdown. With the President's proposal where they have worked up the net retention for each dollar increase, where they came down to 29 cents with the windfall tax versus 43 percent retention without a tax—that sort of gives you—there is a chart that breaks that down, but it's in broad categories, like royalty, severance tax, State taxes, and Federal income taxes.

So, you have four classifications in effect.

There is no question that the Federal tax will go down, because your royalty is going to go up, your severance tax is going to go up, your State income tax is going to go up. Therefore, what is left then after you tax the excise tax or windfall profits tax off and it is currently deducted the way it's proposed. You reduce that. There is a smaller dollar left to be taxed for income tax purposes.

The royalty will run about the same, but with severance tax going up somewhat and State taxes in there, the biggest slice is going to be the windfall profits tax. And when you deduct that, you are going to have a smaller portion of income left to be subject to Federal income tax.

Senator BAUCUS. That's right. That might explain why the effective rate is actually lower.

Mr. SPRINKLE. That's right.

Senator BAUCUS. Well, you know, in all candor, I think part of the problem here is that—I am sure that Senator Wallop will agree—that the problem is going to be some kind of windfall profits tax enacted by the Congress.

That being the case—we can argue the premises—but my point is there probably will be some kind of windfall profits tax enacted by the Congress. If that's so, my question is: How in your view should it be structured? What seems to make sense?

I'm sure you can say, "Well, let's lower it to 2 percent instead of 50 to 60 or something like that." I'm curious if you've got some constructive suggestions.

I do think there is going to be some kind of a windfall profits tax. I doubt if it's going to be the same form as passed by the House. It will probably be less. If your subsequent witnesses this afternoon or later on in the day could come up with some way to fashion the tax, it sure would be helpful, any idea.

Mr. MARTIN. I'm sure there will be some recommendations from subsequent witnesses.

Mr. SPRINKLE. However, as I indicated, you start talking about plowback and it becomes extremely hard to try to draft something that is equitable to the producer. And I think you can go back and you can look at prior years, even with the tax bill proposal there—the problem of trying to draft something there. It's not workable.

You go back to 1974 legislation attempted at that point, it becomes very hard to try to come up with something that is workable. Right now, I have a study that shows that in 1972 dollars, net income after tax per barrel, going back to 1974, net income after tax per barrel in 1974 using 1972 dollars was $3.33. In 1978, it's down to $1.70.

You wonder why drilling is falling off or why people are investing their dollars elsewhere. It gets back to the return on the dollar.

Senator BAUCUS. What is the profit return on the dollar? I mean, Mr. Keating pointed out the oil and gas industry has been lower than the manufacturing industry. What is the rock bottom? To get a high, low and medium rate of return would seem to make sense.

For the industry, what would it be?

Mr. MARTIN. I wouldn't attempt to do that.

Senator WALLOP. Just as a comment, let me tell you what I think about that, because there are some years when the ranch operates at a pretty attractive profit. If somebody finds out, they would be horrified. There might be 10 years that it doesn't operate at any kind of a profit at all.

Senator BAUCUS. The figures Mr. Keating raised is that in 20 years, it has been several percent low. That's a 20-year period. You pointed out what is the low.

Mr. KEATING. Eighteen to twenty percent return on investment would not be unfair, would not be unheard of. The interest rate for investment money now is anywhere from 12 to 15 percent, depending on how desperate somebody is. You should have a rate of return that exceeds the rate of borrowing in order to make a profit and stay in business. If you don't make a profit, you don't stay in business.

Senator WALLOP. I have seen those figures that you read off, Mr. Keating, of the profit increases in various industries. I notice with some interest that I think the television industry is about 600 percent. I'm wondering how they would react if they had a windfall profits tax.

Mr. KEATING. The amount of houses and buildings have gone up tremendously. However, there is no windfall profits tax when somebody is selling a piece of real estate.

Seriously, one thing I would ask you Senators to consider when you go back to discuss this bill, if someone could introduce an amendment to change the name of the bill to an oil production tax rather than a windfall profits tax. I think that would be more honest and fair than anything that you could do, is to give it a proper label.

Senator BAUCUS. I have no further questions.

Senator WALLOP. May I suggest a possibility, after the rest of the testimony, if we have questions that we want to submit to you by mail. And if you agree to answer those——

Mr. KEATING. Certainly.

Senator BAUCUS. Before you leave, I think some of the talk about the plowback provision didn't really apply to the independent, but to the majors—that majors may not use the additional revenue gained through decontrol to produce additional energy. They have to go out and buy something else that is rich enough to do with energy.

Therefore, the thought is: Maybe there is some kind of plowback provision with the additional revenue—additional revenue would be plowed back into additional production. I am glad you raised some problems with plowback. I have been somewhat of a believer to encourage more production. Nevertheless, I think that is one of the reasons why people tend to talk about it, because of the concern.

Senator WALLOP. To the extent it is attractive to make the investment worthwhile I don't think you have to worry about it.

Mr. KEATING. There is a misconception about the majors spending a lot of money, buying up other things.

A very, very minor percentage, less than 1 percent of their value, has gone to buying diversified industry. But as a point of interest, in 1977, the only portion of Mobil Oil Corp. that made a profit was their paper box company. That's what derived the profit for Mobil in 1977.

I hear this business that companies are out buying other industries. And that is a misconception. If it were looked at very carefully, I think you'd find a very, very small portion of the industry is used for diversification.

Senator BAUCUS. I'm sure it's not all related, but as you possibly know, the people of the box company were price fixed.

Mr. KEATING. Another thing I would like to add—it's a personal thing. Senator Jackson went on TV and said the oil lobby was the toughest lobby that he encountered and its incentive was greed. He said that nationally on television. And I would like to correct that statement.

I don't know that we are greedy. I think that we are honest businessmen. And all we want is a fair shake.

Senator WALLOP. Thank you. The next panel is Mr. Dave True, Mr. Warren Morton, Speaker of the Wyoming House of Representatives and Mr. Webb Allen of Palmer Oil and Gas.

STATEMENT OF H. A. TRUE, JR., TRUE OIL CO.

Mr. TRUE. I am H. A. True, Jr., commonly known as Dave. I appear as a partner of True Oil Co. I deeply appreciate you Senators and your staff coming to Casper for this Senate Finance Committee hearing. I am confident that you got some viewpoints, and some concerns, and some situations explained that might not readily be available in Washington.

I have prepared and submitted a written statement. With your permission, I will not read it.

Senator WALLOP. The statement will be entered in the record as if you delivered it.

Mr. TRUE. From what has already been said, it would be somewhat redundant. As a matter of fact, the Senator made my speech for me in his opening statement. And so, I will not repeat it. I will make a few brief statements. And then if you are agreeable, I will try to answer any questions that you and the staff might have.

I have been in this business as an independent oil man for 31 years, first as a drilling contractor, then as wanting to be an oil producer, finally as an oil producer. And from time to time since, I have wished I was in some other business.

During this time, of course, we have seen depletion attacked and seriously restricted, in some cases, eliminated. We have seen serious attacks on intangible drilling costs, in elimination and change of their treatment. We have seen a so-called minimum tax on successful intangible drilling costs.

We have been through a whole series of price controls and have watched the Federal agency regulate the price of crude petroleum in this country to where it resulted in a full $5 billion less to the oil industry than called for in the pricing mechanism that was passed in 1975 by the Congress. We have seen interstate gas regulated for the first time. We have seen tremendous land withdrawals and bar metal restrictions.

Some are certainly helpful and some punitive. I think my statement outlines more specific cases, where I think three of them I list the cost as varying from about $13,000 up to $200,000 that were completely unnecessary and nothing was changed other than the delay.

The four cases that my testimony mentions is still in doubt. We don't really know whether we are going to be able to proceed with that project or not.

We have seen the positive effect of the fact that intrastate natural gas was not controlled pricewise, to where the industry actually built a considerable surplus before the 1978 gas "decontrol bill" was passed.

We saw in the case of intrastate gas a market price mechanism working and the price went up. They developed a surplus for this State's usage. And the price started back down. And we even saw the Department of Energy changing its position completely and urging industrial use of natural gas after the intrastate gas was included in interstate network.

To put some numbers to the windfall profits tax, the price of stripper or decontrolled oil in the State of Wyoming is now such that the President's proposal would result in a $3.25 per barrel tax on that oil.

The House Ways and Means Committee bill as passed would tax each barrel $3.90.

Last year, referring now to the Morgan Stanley forecast that you read, our little company spent 160 percent of its total net income for oil production and exploration. That is in geological, geophysical, and intangible building costs——

Senator WALLOP. 160 percent?

Mr. TRUE. 160 percent. We did that only by borrowing, increasing our borrowing dramatically. And naturally, we can't continue to do that. We won't frankly be able to do that this year.

I would repeat again that the crude oil price decontrol is not really decontrol when it's coupled with the tax that is proposed both by the administration and the House.

The windfall profits tax again has nothing to do with even windfall or profits. I have read the administration's bottom line on what happens within and without windfall profits tax. And I notice that they come up that an unincorporated independent has 29 cents left of each dollar after a 50-percent windfall profits tax. I figured and figured what we would have left here in the State of Wyoming. And at 50-percent tax, we would have 9.8 cents. At the 60-percent figure proposed by the House of Representatives, we would have 6.3 cents.

Senator WALLOP. Could you make those available to us sometime so we can use them?

Mr. TRUE. I certainly will. I will give you a breakdown.

Let me again repeat that there is no way that this country can control the delay, harass or conserve our way to energy self-sufficiency or energy independence. The only way to do it is to produce. And that's what we are basically asking for a chance to do.

Thank you very much.

[The prepared statement of Mr. True follows:]

PREPARED STATEMENT OF H. A. TRUE, JR.

I am H. A. True, Jr., Partner in True Oil Company and I reside in Casper, Wyoming.

It should be made crystal clear that the title of the two proposals to be discussed today are entirely specious and have been so labeled to fool the public:

Crude Oil Decontrol.—The price of crude oil is not being decontrolled by the actions seen to date by the President and the House Ways and Means Committee. Factually, under these two proposals price controls will continue on crude oil forever.

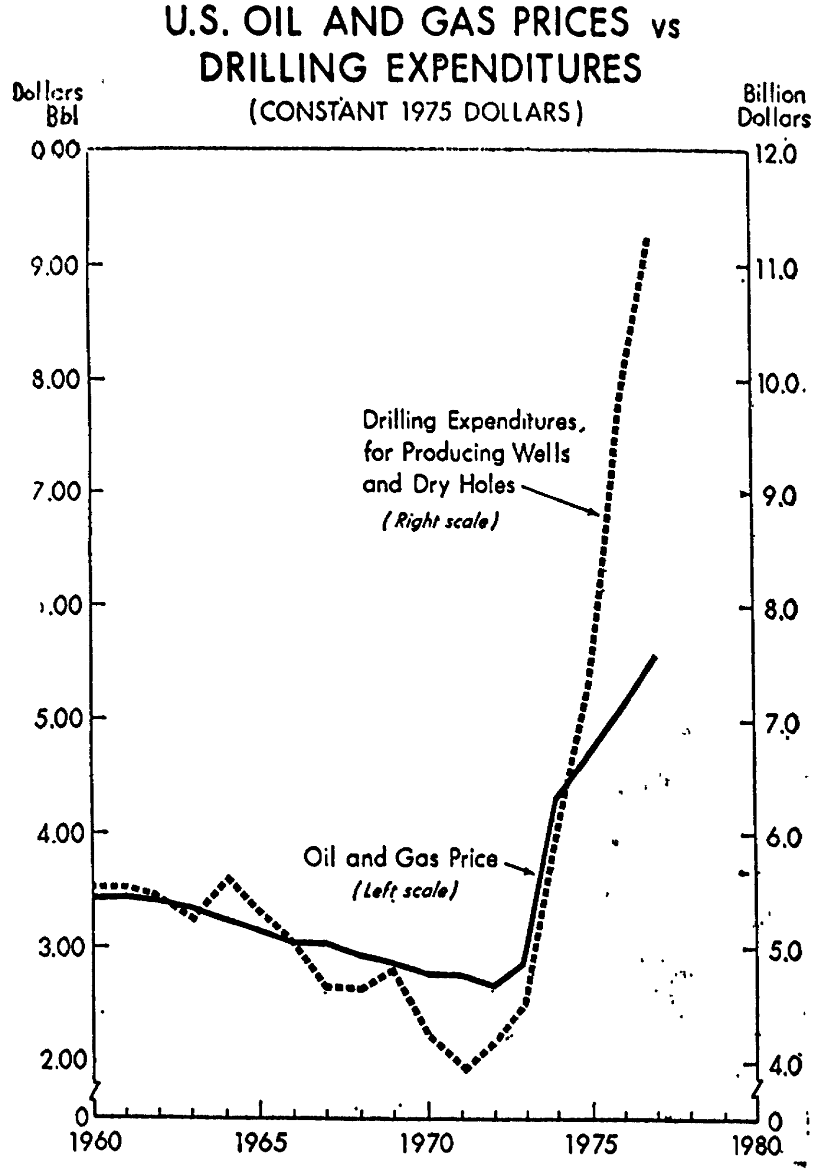
Windfall Profits Tax.—The proposed tax by President Carter and also by H.R. 3919 is not a tax on profits at all—it is a pure and simple excise or sales tax on the wellhead price of crude oil.

A basic economic fact of the law of supply and demand has been demonstrated effectively in the last eight years by government price controls on crude oil. Anytime the government puts price controls (maximum prices) on a domestically produced product, then it naturally follows that there will be a shortage of this domestically produced product. This has certainly been the case of crude oil in the past eight years. In just the past five years our imports of crude oil have gone from 30% to 50%. The majority of these imports are coming from extremely politically unstable countries.

It seems to me that the best way to get our country back on track towards achieving self sufficiency in the energy field is to decontrol crude oil and not to impose any sort of sales or excise tax on the production of crude oil. During the past eight years the oil and gas industry has invested in their next year's exploration and drilling budgets more than was made in profit during the prior year. It seems to me that instead of the government wanting to tax the oil industry they should instead be trying to pass laws that would give even greater incentives to explore, drill for and discover new crude oil reserves to reduce our growing dependence on such unstable political states.

In 1973 when the price of crude oil was approximately $2.85 per barrel industry expenditures were only $4½ billion per year, however, in 1977 the average price of oil had increased to approximately $5.55 per barrel and industry expenditures grew to $11.3 billion per year (in constant 1975 dollars—chart attached). This once again proves the economic fact that when a material is in short supply the producers of that material will exert all of their mental, physical and financial resources to increase the supply if a reasonable profit can be made by producing the material.

Even with this tremendous increase in drilling and exploration during the past five years, which was due to the increase in the price of crude oil, our reserves of crude oil are declining because of the extraordinary increase in demand for crude oil and its by-products. It should be pointed out that since the fall of 1978 when the Natural Gas Policy Act was passed a dramatic slump in drilling activity has taken place. This was due primarily to inadequate wellhead revenues because of the Energy Policy and Conservation Act, the confusion and uncertainty brought on by the passage of the Natural Gas Policy Act of 1978 and the terribly high inflation costs which have existed in the oil industry (chart attached). The administrators of EPCA have limited oil industry revenues from crude oil sales to $5 billion less than the amount authorized by Congress. The Natural Gas Policy Act of 1978 put price controls on intrastate gas for the first time ever and, in addition, created a total of 27 different prices for natural gas—this Act has created utter confusion and fear of the unknown amongst the industry and the situation will not be straightened until FERC clarifies the myriad of rules and regulations of this disastrous Act. The reversal of this drilling decline can now only take place by Congressional action which will carry out the program proposed by the Independent Petroleum Association of America which calls for decontrol of upper tier oil effective June 1, 1979 and phased deregulation of lower tier oil by October, 1981 as spelled out in EPCA. This decontrol would have practically no negative impact on the economy—the estimate being 0.1% impact on inflation in 1978, 0.3% in 1980–81.



The above once again stongly verifies the point that when prices and production of a commodity are controlled by government, a shortage of that commodity will be created. Historically, government officials feel that they can control the supply of commodities at a "fair" price much better than the citizens, so they blame the citizens for the shortages—just as the President is doing today regarding the gasoline shortage—and set up a system of price controls. Since the ancient times of Babylon, 4,000 years ago and up to the present time, price controls have been put into practice every generation or so and invariably they fail and are allowed to die with no fanfare.

50-872—79——3

COST INDEX OF DRILLING AND EQUIPPING WELLS

[Unadjusted for depths 1974=100]

	Weight (percent)	1973	1974	1975	1976	1977	[1] 1978	Percent increase 1977-78
Payments to drilling contractors	36 6	77.0	100	120.0	131.1	[2] 157.1	178.6	13.7
Purchased items:								
Road and site preparation	4.1	93.2	100	110.8	119.4	128.7	133.8	4.0
Transportation	3.9	90.1	100	108.8	115.4	123.6	140.6	13.8
Fuel	1.1	57.2	100	121.6	141.3	[2] 171.4	183.3	6.9
Drilling mud and additives	6.9	84.4	100	127.7	143.4	151.1	179.2	18.6
Well site logging and/or monitoring system	1.2	87.7	100	117.5	126.1	136.2	154.5	13.4
All other physical tests	.7	88.4	100	120.3	135.4	148.7	163.5	10.0
Log and wireline evaluation services	3.2	89.8	100	118.1	137.9	152.5	175.0	14.8
Directional drilling services	.6	87.7	100	106.6	116.3	126.2	141.3	12.0
Perforate	1.1	89.8	100	118 3	131.0	143 1	155.2	8.5
Formation treating	3.0	93.4	100	126.6	137.3	144.0	154.3	7.2
Cement and cementing services	3.7	92.1	100	124.6	133.7	137.1	152.4	11.2
Casing and tubing	17.5	73 6	100	111.2	120.3	132.6	147.6	11.3
Casing hardware	.7	73.6	100	111.2	120.3	132.6	147.6	11.3
Special tool rentals	3.1	89.8	100	115.0	127.2	139.1	153 1	10.1
Drill bits and reamers	1.6	87.7	100	124.3	134.3	147.9	165.6	12.0
Wellhead equipment	1.8	85.6	100	120.5	141.5	165.2	184.2	11.5
Other equipment and supplies	2.0	84.4	100	124 4	138 0	149.9	165.7	10.5
Plugging	.5	93.1	100	115.0	122.0	128.0	140 3	9.6
Supervision and overhead	2 1	87.8	100	110.8	119 5	129.3	143.8	11.2
All other expenditures	4 6	81.9	100	111.5	118 5	126.9	136.1	7.2
Subtotal purchased items	63.4	83.5	100	116.4	127.4	[2] 138.3	154.0	11.4

[1] Preliminary.
[2] Revised.

Sources: Weights from IPAA Cost Study Committee Survey of distribution of expenditures in drilling and equipping wells in 1974. Index of payments to drilling contractors from IPAA Annual Survey. Price indexes from Bureau of Labor Statistics and other Government publications, and data provided IPAA Cost Study Committee by service and equipment companies.

Natural gas, crude oil, and their by-products are the only commodities to my knowledge on which there are still statutory price controls. It's time they are removed to let the free enterprise system work to start increasing our reserves of oil and gas.

It is estimated that the increased revenues to producing companies would bring forth new production of more than 400,000 barrels of oil per day by 1981 and approximately 2,000,000 additional barrels per day in 1985.

High inflation and high costs for exploration and drilling are some of the major reasons for the decline in the discovery of new crude oil reserves. I would like to strongly point out that one of the major reasons for the high costs and high inflation in the oil field industry are the delays and harassments by Federal government agencies.

The Department of the Interior, through its regulations has had a tremendous impact of the industry. But let's see what has happened through the Department of the Interior and its rulemaking regulations. A couple of years ago Interior came out with what was called "The List of 13," which was thirteen requirements for obtaining approval of a drilling location on the public lands. It was quite detailed and onerous and took a lot of time. We hadn't seen much of anything though, because in 1975 Interior came out with the NTL-6 which is a whole laundry list of not only what you have to do before drilling, but what you have to do during drilling and after drilling.

I'd like to relate a couple of horrible examples of what has happened to us under these regulations. We staked a well location in North Dakota where the Federal Government controlled the surface and the mineral rights. We invited personnel from the Forest Service, the U.S. Geological Survey, and the Bureau of Land Management into the field and got the location approved. We thought everything was fine. The first load of the drilling rig arrived and as it turned off the county road, 660 feet from the location, a "Keystone Cop" in the form of a district engineer for the USGS came up and shut us down because nobody had approved the road to the drillsite. So we had to send for the engineers to make a cut-and-fill profile and do all the other engineering. After all that we just drove over the prairie, but we did finally get approval. We estimated that that little misunderstanding cost us a cool $25,000.

In early November, 1976 we made an agreement with a lessee to drill on his Federal lease, which was due to expire on January 31, 1977, some eleven or twelve weeks later. As you may know, the USGS is very stuffy about extending leases for two years. To get an extension you must have a rig on the site and be drilling on the expiration date. For this reason we made an allout effort to get approval of the location. Our first visit to the location, accompanied by USGS personnel, dirt contractors, engineers, and geologists, was on November 12, 1976. The USGS approved the location but the BLM did not.

We then staked an alternate location 600 feet northwest. Let me explain that up in this area you are sharpshooting at little pimples. They are one-well oil fields and, if you get off the closure and away from the porosity, you get a dry hole. It is a very scientific pinpoint process. We finally agreed to move 600 feet northwest in order to place the drillsite in a different environment on the National Grasslands. We resurveyed it and on December 12, 1976, got everybody back together to reexamine the location. Again the USGS approved but the BLM did not. One week later we received a list of reasons for refusal: (1) the access road required too much cut; (2) the location required too much cut; and (3) the area was identified as a critical area for raptor nesting sites. Furthermore, the previous lessee had built a road within a quarter of a mile of our location which we had planned to use but we had not requested permission to do so. As a result, the whole deal was again turned down. The final objection was that the access road—and this was in rough, rugged country—would require more than a two-foot cut. You can hardly build an access road on a prairie with less than a two-foot cut!

Finally, on January 4, 1977, a third wellsite inspection was made at a new location, forty or fifty feet away. On January 18, we received the necessary approvals. Because of a shortage of rigs and because we had to have a rig on that location and drilling by January 31 in order to extend the lease, we had been paying standby time for a rig since December 1, 1976. We force-drafted equipment into North Dakota and got the road and location prepared. The rig began drilling about six hours before the deadline, and we got the extension of the lease. Unfortunately, this all turned out to be a mistake because it was a dry hole. If we had just known that, we would have happily lost the lease and saved the money. We have documented the cost of that delay on the location at $200,000. Now that's pretty expensive hawk-nesting protection.

For example, we were drilling a well for Atlantic Richfield approximately 50 miles southwest of Casper on "Bald Prairie" Federal lands. Atlantic Richfield had filed all the necessary papers to obtain permits to drill the well and our rig was moved on location and started drilling. A few of our rig workers could not find locations to park their small camper trailers anywhere within 75 miles of the rig, therefore, permission was requested to park the camper trailers on the well location from Atlantic Richfield and the rancher who has an operation on this land and they both gave permission. When the USGS heard that the camper trailers were parked on the rig location they shut the drilling operation down for two days—this cost our company over $9,200 per day in lost income from the rig plus wages paid to the rig workers.

Another example of government agency delays is our Deadman Unit in the Overthrust Belt in western Wyoming. We have been trying to get a permit to drill this unit since last September 1978 but have been unable to do so. We feel that this unit has great potential to discover oil and/or gas reserves to help resolve the energy crisis for our country but once again we are being hindered in our efforts by government agencies rather than being helped by them.

Many other examples of this type are available from drilling exploration or producing companies operating on "public lands" adminstered by government agencies.

The amount of money required to increase our reserves of crude oil so that production can be increased and thereby reduce our dependence on imported crude oil is mindboggling—somewhere over $50 billion per year in the 1980's as pointed out in the June 26, 1979 issue of The Oil Daily quoting the Bankers Trust Company study. I believe after reading this article you will agree that complete decontrol of crude oil prices without a "windfall profits tax" is absolutely necessary and is the best Congressional action that could be taken in the best interest of our country. (Copy attached.)

[The Oil Daily, Tuesday, June 26, 1979]

INDUSTRY PROFITS NOT EXCESSIVE, STUDY SAYS

(By Sharon Gamsin)

NEW YORK—Oil industry profits are far from excessive now, and even with decontrol, would likely remain well below levels needed to fund the type of exploration drive needed just to maintain current production levels, a study by the Bankers Trust Co. concludes.

The bank's economists estimate that just to sustain the current production rate would require real capital expenditures of $40 billion to $50 billion a year in the 1980's—more than twice the $20 billion annual investment rate of the past few years.

That means 15 to 20 percent of the nation's fixed investment expenditures by 1985, from about 10 percent in 1978 and only about 7.5 percent in 1972. That's a whopping increase, but the bank believes it can be done without a "traumatic impact" on the U.S. economy.

They point out that if oil and gas expenditures were to rise to $40 billion or $50 billion by 1985, those expenditures as a share of GNP would rise from roughly one percent today to 1½ to 1¾ percent by that year—not a major upheaval at all.

But before investment in oil and gas producing facilities can rise to that kind of level, the industry's profit and rate of return will have to rise, too, the bank says.

Although the gross revenues of the top 25 oil companies have far outpaced non-oil firms, the bank finds that "where it counts, in net profits, the oil companies were outpaced by the other firms."

The non-oil group averaged 10.1 percent annual profit growth during the 1969 to 1978 period against 8.1 percent for the oil group. Moreover, the bank points out, when the oil industry reinvested its profits, it found that costs in the industry were rising by 9.4 percent a year.

"In fact, the industry's profits are neither obscene, excessive, nor even particularly unusual, by any reasonable standard," the report states.

NO 'OBSCENE PROFITS'

The bank also found that the industry's rate of return on invested capital "fails to warrant the charge of obscene profits."

The oil industry's return on capital, at 9.3 percent, averaged less than one percent more than that of the non-oil industries in the 1969–1978 decade. In the last three years, the report notes, the petroleum industry's return on 8.9 percent has been one percent below that of non-petroleum industries.

Shifting emphasis to the return on stockholders equity makes the industry critics case even less credible, the bank says.

In the last three years, the industry's return on stockholders equity, at 12.5 percent, is 1½ percentage points below the national average.

"In short, the rates of return in the petroleum industry have been so unexceptional that there would be no reason to mention them were it not for the undue public attention they have been given. Actually, the rates of return are remarkably low for an industry that is expected by its critics to do so much more," the report says.

In fact, it continues, "because profits have been inadequate, the industry has had to increase borrowings to finance huge expenditure gains. Consequently, the industry's debt-to-equity ratio in the last three years has averaged 40 percent, an all-time high."

According to the bank's estimates, decontrol won't go far in providing additional funds for exploration. If producer revenues rise by the $10 billion to $15 billion estimated by the government, taxes would reduce earnings to somewhere between $4½ and $6½ billion without the "windfall profits tax" and between $3 and $4½ billion with it.

NOT SO IMPOSING

"While the additional profits are huge in absolute terms, they are much less imposing when compared with the incremental capital requirements expected," the bank's economists note.

"The critics who charge the industry with having 'obscene profits' are obviously unaware of the industry's track record in recent years," they continue.

In short, Bankers Trust Company believes, "the unceasing attacks on oil profits are not only erroneous, but they also divert attention from the real need for higher profits that are required to serve the national interest."

"The 'windfall profits tax' reflects an inappropriate concern with profits in the oil industry," the report concludes. "The debate over profits obscures the main issue, which is how to minimize our reliance on foreign oil supplies. What is needed is less debate on how to get petroleum profits down, and more effort to get production up."

Our company's intangibles (drilling and development) costs in 1978 were 160% of our net production income. This should further serve to indicate that independent oil companies are in fact reinvesting their profits in exploration and drilling development to increase our domestic crude oil reserves.

With the tremendous amounts of money required to explore for, drill and develop crude oil reserves it is patently clear that we need all of the profit we can make to reduce our dependence on politically unstable OPEC countries. If a 50% windfall profits tax is passed, this would leave a Wyoming independent oil producer in the 70% Federal income tax bracket only 18.8¢ out of each additional dollars income due to decontrol. If a 70% windfall profits tax is passed, this would leave the independent producer only 16.7¢. A form is being attached which shows this information along with an example which was supplied by the U.S. Treasury Department and included with the White House Fact Sheet released April 26, 1979. It is crystal clear that the only entities receiving a windfall are the State and Federal Governments—certainly the independent oil producer is *not* receiving a windfall profit.

Another point to consider is that oil fields do have a decline rate and in addition to finding new reserves to replace imported crude, we must also find enough new reserves to replace production from old oil wells which are declining at a rapid rate. The cost of finding these type reserves is the same as it is for finding any other new reserves of crude oil.

At the present time approximately 75% of the United States energy consumption is supplied by oil and gas—oil supplies approximately two-thirds and gas one-third. As you know, we import approximately 50% of our total energy requirements, therefore, it is quite evident that 25% of our total energy requirements depend on imported crude oil. In my opinion, to put it mildly, it is certainly less than intelligent to have 25% of the U.S. energy requirements dependent on the extremely unstable countries in OPEC.

If a "plowback" could be so constructed as to be completely equitable to all individuals and companies, I would certainly find no fault or would not argue that action.

Item	Amount	
Impact on typical unincorporated independent:[1]		
Without windfall tax:		
Amount	$1.00	
Royalty	−.14	
	.86	
Severance and property tax	−.102	
	.758	
4-percent State income tax (not applicable in Wyoming)	NA	
	.758	
70-percent Federal income tax	.531	
Net to producers	.227	
	Windfall tax	
	50 percent	70 percent
With windfall tax:		
Amount	1.00	1.00
Royalty	−.14	−.14
	.86	.86
50-percent windfall tax	.43	−.602
	.43	.358
10.2-percent severance and property tax	−.102	−.102
	.328	.256
4-percent State income tax	NA	NA
	.328	.256
70-percent Federal income	−.23	−.179
Net to producers	.098	.077
Adjustments to reflect revenues from released lower tier oil not subject to lower tier tax	+.09	+.09
Overall net to producers through Oct. 1, 1981	.188	.167

Item	Amount
Estimated effect of taxes and royalty payments on revenue increases to producers:[2]	
Without windfall tax:	
Amount	$1.00
Royalty	−.14
	.86
Severance tax	−.05
	.81
4-percent State income tax	−.03
	.78
45-percent Federal income tax	−.35
Net to producers	.43
With windfall tax:	
Amount	1.00
Royalty	−.14
	.86
50-percent windfall tax	−.43
	.43
Severance tax	−.05
	.38
4-percent State income tax	−.02
	.36
45-percent Federal income tax[3]	−.16
Net to producers	.20
Adjustments to reflect revenues from released lower tier oil not subject to lower tier tax	+.09
Overall net to producers through Oct. 1, 1981	.29

[1] Example prepared for producer in Wyoming where State severance tax is 4 percent and property tax is 6.2 percent of wellhead value. A 70 percent marginal Federal income tax rate is used.

[2] Example supplied by U.S. Treasury Department.

[3] A 45 percent marginal Federal income tax rate is used here because it is applied to taxable rather than gross income.

To summarize—my recommendation is to decontrol all upper tier oil as of June 1, 1979; phase out decontrols on old oil as of September 30, 1980 and do not impose any sort of so-called windfall profits tax.

I believe that it is wise to remember that we cannot control, delay, harass or conserve our way to energy independence in the United States in these days of crisis—there is only one way that we can become energy independent and that is to produce our way to energy independence.

Thank you very much for allowing me this time.

Senator Wallop. Thank you. Mr. Morton?

STATEMENT OF WARREN A. MORTON, SPEAKER, WYOMING HOUSE OF REPRESENTATIVES

Mr. Morton. Senator Wallop, Senator Baucus, my name is Warren Morton. For all my adult life, I have been involved in the independent producing segment of the oil and gas industry. For the past 13 years, I have served in the Wyoming Legislature and presently serve as speaker of the house of representatives. My comments today result from my long involvement in the interrelated business of energy and politics.

The apparent issue before the Congress today is the proposal by the President, as expanded by the House, to place an excise tax on the gross revenue derived from the President's proposal for phased deregulation of crude oil prices. However, the real issue before the Nation today is: Will the people and the Government of the United States have the honesty and courage to recognize the worldwide, not national or local, but worldwide energy crisis and take meaningful steps to meet and eventually resolve this problem?

I would hope from the meetings that were held last week in Geneva with the economic summit that the problems of the world we recognize as being from the point of supply—namely the OPEC nations—and not try to lay the defeat of the domestic industry.

Fortuitously for this Nation, we have the resources to provide a solution to this problem. All we lack is the resolve to face a very difficult decision.

It should be clearly understood that the problems of today's energy crisis are not the result of actions or nonactions of this administration or Congress, but indeed for over 25 years.

During the Eisenhower administration the dangers of overdependence on foreign oil, particularly oil that originated in an area as remote and potentially unstable as the Persian Gulf, was clearly recognized. And efforts were made to restrict imports to 12½ percent of daily consumption.

However, through the years, the political pressure to utilize what was then referred to as cheap Arab oil proved an irresistible temptation to each and every subsequent administration and Congress, with the result that our dependence has grown to nearly 50 percent. And the Arab oil is quite obviously no longer cheap.

So much for history. What can we do about it now? It would be my fervent hope and recommendation that as the Congress faces decisions dealing with energy that you look beyond the obvious problems as represented by high prices and long gasoline lines, and base every decision on the premise: "Will this action improve either the short-term or long-term supply of energy for this Nation?"

Let me assure you that H.R. 3919, the so-called windfall profits tax bill, does neither. Allow me to elaborate.

The first requirement for any piece of legislation should be that it is both understandable and enforceable. H.R. 3919 is neither. It is an incredibly complex piece of legislation involving references to tier I, tier II, and tier III pricing schedules further complicated by variable decline rates of sometimes 1½ percent, sometimes 2½ percent, and sometimes neither, sometimes coupled with a 2-percent inflation adjustment and sometimes not, with special provisions for Alaskan oil, oil derived from State lands, which I might add, provides for the first time a Federal tax or bite in the State's income from State lands, an item of more than passing interest to two Senators from the West, and finally topped off with a 50, 60—I don't know what the figure is—percent tax on gross income with no thought to consideration given to the cost of either discovery or production.

I had 70 percent in my paper. Maybe it's 60 percent now. I am critical of any of them.

Certainly nothing within this bill would do anything to alleviate either the short-term or long-term supply of oil to the country.

By the way, Senator Baucus, you asked for a breakdown of where those dollars fell. Here's a copy for you, showing the breakdown, taxes, and so forth. You might find them helpful.

To meet the ever-increasing cost of frontier exploration today, the issue is best met by no new or additional taxes at all. For example, the oil industry in Wyoming today is watching with great interest a well currently testing below 25,000 feet. This well has already cost in excess of $15 million. The Nation can ill afford to withdraw funds from this type of exploration to satisfy short-term political goals.

However, having said this, I am enough of a political realist to know that the Senate must respond to the House action on the President's proposed excise tax. And I would propose the following specific alternatives.

It is a well established statistical fact that the burden of domestic exploration is carried by the independent segment of the industry. These operators use, in part, their own internally generated funds but also depend heavly on outside, private investors by utilizing limited partnership agreements.

The proposed new taxes would absolutely destroy the incentive for new exploration by these independents unless some sort of "small producer exemption" could be established. This has been done in related tax matters in the past. And I would recommend an exemption of the first 1,000 to 1,200 barrels of daily production for any new tax proposal to be considered by the Congress.

Recognizing that the prime purpose of the President's move to deregulate crude prices is to stimulate the search for new production, the 70 percent, 60 percent, or 50 percent tax proposed by the House is absolutely counterproductive unless it is accompanied by a provision to plowback these new revenues into new exploration.

If the tax must be applied it should only be applied after deducting the expenses incurred in new exploration such as land acquisition costs, geophysical expense, and all drilling expenses. If such a plowback provision seems to be too cumbersome to enforce, the same goal could be attained by applying a tax to what the Congress determines to be excess profits.

Quite obviously, such a tax should encourage the maximum reinvestment by the industry into new and expanded exploration and should be a tax on the remaining profits, not a 60-percent cut of gross revenue produced.

All of the above recommendations deal with efforts to alleviate the near-term shortfall in petroleum supplies. However, I feel I would be derelict in my responsibilities if I did not address the fortuitous circumstances that provide this Nation with at least the opportunities for a long-term solution.

I refer, of course, to the development of a synthetic fuels industry derived from the virtually limitless supply of coal and oil shale in the United States, most of it located within the States of Montana, Wyoming, Colorado, and Utah.

Let me put these reserves in perspective. The known free world proven oil reserves, including all of the Persian Gulf nations, is approximately 565 billion barrels. Realizing that figure conflicts with the figures of the Mexican reserves, I challenge the Mexican figure.

The shale oil reserves of the Rocky Mountains is conservatively estimated at 1.8 trillion barrels. And if this is upgraded to the deposits containing 25 gallons per ton, the recoverable reserves are estimated at 600 billion barrels. The coal reserves of these four States alone represent the oil equivalent of 515 billion barrels of oil. By the way, daily oil consumption in the United States runs 18,000 barrels.

Do not forget that the German war machine during World War II was virtually 100 percent supplied by synthetic fuels from coal. The technology for the development of either or both of these synthetic fuels has been known for years. Africa is going to complete synthetic fuels from coal.

What has been missing is a national resolve to realistically face the cost of these synthetic domestic fuels. Whether viewed from a military standpoint or based on the economic survival of this country, this Nation can no longer afford to be held captive by foreign oil interests.

If you wonder, by the way, what the cap is on OPEC oil prices, it's the price at which these things become effective, which is the $25 to $30 range.

These fuels cannot be developed under the artificial constraints of price control. Both systems start to become competitive at a price of $25 per barrel. This development should be financed by private capital, using earned profits from other sources, possibly subsidized with a temporary $2 or $3 per barrel allowance, encouraged by favorable depreciation schedules and unencumbered by unnecessarily restrictive environmental standards.

Long terms, there really is no viable alternative available to the Nation. The only question is will such a program begin before it is too late.

The Congress will face decisions that deal with our energy supply in the next few months. In my opinion, the very survival of the Nation is at stake. I trust and pray that the decisions will be made by statesmen and not by politicians.

I thank you for the time.

Senator WALLOP. Thank you.

Mr. Allen?

STATEMENT OF WEBB ALLEN, PALMER OIL & GAS

Mr. ALLEN. Senator Wallop, Senator Baucus, panel, I don't have a prepared statement. I can type this up and leave it with you.

Again, a lot of the things that I have said here have been said. And so, I will just comment on some of the things that I think that somebody may have overlooked or that I think need to be said over and over again.

Basically, when the administration proposed the decontrol program, they stated that the reason was to give the industry the incentive to go out and find more oil and gas reserves, increase our supplies. But at the same time, they proposed to tax away 50 percent of it.

It seems to me that in order so that the oil company didn't have to get any excess profit—it seemed to me that if they had control of the decontrol program, why would they have to decontrol and take back half of it? They could have stretched out the decontrol program a little longer.

I think what they really are doing is simply trying to raise money. And this is a very bad way to do it. They are trying to raise revenue.

They have already got in place an excise tax at the gasoline pump. If they want to curb demand that way, all they have to do is increase the rates. They can raise a revenue for alternate energy projects that they think they ought to invest in, Government ought to invest in. There is no additional administration involved in it.

Senator WALLOP. You are suggesting they tax the consumer?

Mr. ALLEN. It's the consumer that is going to pay for it—I mean—immediately when that tax goes into effect. It's not the oil producer. The consumer is going to get the bill the day the tax goes into effect.

And I think it was just a left-handed way of making him like it, because it made him think they were actually taxing the producer. The producer is not going to be having to pay the tax. He is going to have to administer it, have to put up with it.

It's going to delay the time he is going to be decontrolled. He is not going to get the revenue it's going to need. But the country is going to suffer if the oil producer doesn't get the necessary funds.

Decontrol is a good incentive, but without the funds, its meaningless.

I think the administration is just using a sneaky way of getting the consumer hit with the heavy tax and making him like it. That's my opinion of it.

If they want to tax the consumer, very well. If they want to curb the demand, they can put it at the filling station on the pumps, diesel pump, or home heating oil, if they wish. But this is a bad way to do it.

I mean, producers are already strapped with all kinds of regulations. Along that point, there is a lot of little independent producers in this country—I mean, they aren't incorporated—some of them are—but the guy is a geologist and out there trying to find some oil. He's got his wife doing the paperwork part of the time.

When he gets into these complicated rules and regulations, he has got to hire a lawyer and an accountant. He has got to shut down what he is doing.

There is a lot of little areas of very marginal production. These people become very effective in trying to solve our energy crisis. They go out and put a lot of small deals together. They shut down completely when they are faced with this kind of regulation.

This natural gas tax was a good example. I don't think any of these people spent very much time this last winter trying to solve our energy problem. They were trying to comply with the regulations. A lot of the time a lot of technical people had to be tied up in that process of reporting and making those applications for price and control.

A lot of technical people were brought in out of the field just to handle that paperwork.

I don't think anybody knows how this tax will finally be enacted, but because of the changing prices every month, it's got to be complicated, got to be very difficult to administer. Somebody is going to come along and audit it.

Naturally, it diminishes the funds that the producers will have to go out and find oil and gas reserves. The fears that people give that the oil and gas companies will make a lot of profit if you don't come back and tax them—I think history shows what the independents, even the majors—it takes a lot of capital. And if they don't spend that money, if they don't reinvest in exploration, research, we have already got in place a plowback provision.

Our income tax—they are going to have to pay 50 percent of those dollars that they—we don't even need a plowback provision. If they don't spent the money, they are going to get relieved of 50 percent of it, at least.

So, I don't think we need anything insofar as the profits. I don't think anybody has to have any fears of what they will do with their money.

All these decontrols and all these funds—if we don't have this tax, it's going to be more money over a period of 2 and 3 years. It will come on stream and be available.

I think somebody mentioned where are we going to spend these dollars. If we got all of our very highly potential areas tied up in some study that may go on for 10 years—I think that problem has to be resolved, too. That's a big drawback to try and expand our exploration program.

A lot of harrassment is involved in trying to get anything done. I think that somebody pointed out something I wanted to say. We have learned an economic lesson, a simple lesson in economics, I should say, recently when the natural gas prices were increased in 1976.

At that time, our supplies were depleting quite rapidly. The Federal Power Commission which governed the natural gas prices at that time raised the price 178 percent overnight, just one big increase. Within 2 years, we have a surplus of natural gas. And I think there is a lot of evidence—because of that big increase, you are seeing a lot of people conserve natural gas.

I think our consumption was down last year. And the price did this. It solved the natural gas problem within 2 or 3 years.

We are not increasing oil prices 178 percent, but if we have a substantial increase—and the important thing, I think, is if the producer knows he is not going to be continually controlled. If he thought we were going to have decontrol and his confidence was such, I think that—it's really unknown how many barrels of oil we can find in this country, but I think there is a lot of potential of even existing reserves that are really economical at this time.

I think that as the price of oil went up, maybe we wouldn't find the conventional fuel within our borders sufficient to last us forever and ever, but again, some of the other fuels, coal, shale oil, when that price gets up there, somebody is going to figure out how to make that economical someday. They are going to have an incentive to do so.

Up until this point, why would anybody spend a lot of money on trying to produce shale oil if they couldn't see down the road they were going to be able to profit.

Senator WALLOP. Let me ask: If we achieve that moment when those come on line, would that be a moment when competitive circumstance would return to the energy market?

After all, while we are all talking about supply, at this moment in time there is no such thing as a competitive market. That's the reason OPEC can virtually do what they want to do.

And sooner or later, I think part of our job is to look down the road and find out at what point the competitive circumstance would exist so the levering ratchet effect of a variety of influences on our energy market now would cease and we would get a competitive circumstance.

Mr. ALLEN. I think, as our oil prices go up, people are going to conserve. We don't have to live at our cabin 40 or 50 or 60 miles away from our job. People do this, drive back and forth.

I can go down to our high school in Billings, Mont., any day of the week. And it is chuck full of kids driving cars to school. It still is.

Senator BAUCUS. Let me add here something that is somewhat fictitious. Senator Cranston says that California helped solve the energy crisis and, at the same time, contended with the 55-mile-an-hour speed limit. They simply abolished the 55-mile-an-hour speed limit. Now people in California can only go as fast as their age. So that slowed down teenagers considerably.

Also, it helped older people get more quickly to where they are going because they haven't got much time to get there. And in addition to that, it's helped conserve fuel, because no woman dare drive over 35 miles an hour.

Mr. ALLEN. Good point. Well, that's really—it's just an economic situation. I think that you are going to see it in the natural gas situation. Natural gas is becoming very expensive. People's heating bills are getting expensive so people are going to insulate and fill in the cracks. And they are going to do something about it.

If you allow these prices to seek the demand level, a lot of your problems are over. I mean, you can cut hamburger prices to 25 cents a pound at the meat counter and people will start feeding it to their dogs. They may already. But as soon as the supply runs out, you got a big fight in front of the meat counter.

Of course, the butcher gets butchered.

Senator WALLOP. First of all, Mr. Morton, I want to commend you for your statement. I think it's excellent.

Mr. MORTON. Thank you.

Senator BAUCUS. I think it's a very good statement of the problems that face the country. I tend to agree with most everything you say. I wonder if you could expand a little on the small producers' exemption. You say about the first 1,000 or 1,200 barrels of daily production. Would you exempt smaller producers entirely, or would you apply different rates or——

Mr. MORTON. I would just suggest that the first 1,000 barrels of daily production of any operator be exempted from any such excise tax that you might subsequently apply.

Operators who have less production, that would mean all their production would be exempted.

For major oil companies as the so-called seven sisters, you give them the same treatment. You exempt the first 1,000 barrels, also. That would eliminate any discrimination. If you don't give an opportunity for the independent who particularly is topping the private sector, a group that Senator Wallop was referring to earlier—if you put an effective ceiling on their income by 50-percent tax at a frozen level—and you read the proposed bill that comes up to a certain level—and they take it all above there, you let all this cause run unencumbered.

Obviously, with 50- or 60-percent restraint on income and no restraint on expenses, there will come a time when the curves rise and expenses will exceed the income. There is no incentive to invest your money in that situation.

Senator BAUCUS. Your statement says that the independent operators use in part their own internally generated funds but also depend heavily on outside, private investors by utilizing limited partnership agreements.

It would be helpful if you could explain from what sources and what percentage allocation do independents get their financing?

Mr. MORTON. By their own ingenuity and sweat.

Senator BAUCUS. How much is internal? How much is limited partnership?

Mr. MORTON. I will let Mr. True respond to that. No, he doesn't use any outside money at this time. A lot of people who are sitting behind me do.

Senator BAUCUS. Is there any rough figure?

Mr. TRUE. It covers the entire spectrum. Some operations don't put any of their own money in it. And the other side of the coin is that there are operations such as ours that operate entirely on internally generated and borrowed funds.

Senator BAUCUS. What is the difference? Why do some operate entirely outside and some internally?

Mr. MORTON. It depends on your own means, I'd say.

If I could internally generate money to meet all my exploration ambitions, I don't need any outside money. If my production is small, I go out and try to raise money from the private sector to generate my exploration budget.

Senator BAUCUS. To what extent do you borrow from the majors or have to enter into some kind of agreement with the majors?

Mr. TRUE. Well, there are a number of different things. There are some very, very large independent operators that do use outside funds almost entirely, partnerships and public funding and one thing or another.

We do often times get dry hole contributions from the majors or from other independents. We often times have joint projects where we own a percentage and maybe three or four other companies who are operating as independents own a certain percentage up to the 100 percent of the working interest.

So, there are numerous ways. There are bottom hole contributions, dry hole contributions, acreage contributions to support exploratory drilling.

It's not just a matter of where the independents own funds come from.

Senator BAUCUS. I respect your statement, Mr. Morton, that you seem to imply an inclination—express an inclination toward a true excess profit tax if there is going to be tax at all compared with excise tax as proposed by the administration. I guess my question is whether you think that will be any less complex and cumbersome compared with some of the complexities of the bill.

Your statement says how cumbersome the proposal is. It just seems there has got to be 1,500 exemptions——

Mr. MORTON. Let me elaborate. Already, they currently calculate your tax and you pay an income tax thereon. So, the structure exists for the calculation of your tax on your profit. And I hope it will restrict the taxes. And I hope you would also keep my alternatives in proper sequence there.

My first priority is no new tax at all. If you must go the other way, let it be a tax on profit rather than let it be a tax on excise, on the gross. And if the plowback provision isn't acceptable—and I'm aware of the complications. It's a much easier complication to propose than it is to enact.

You already have a Federal structure to calculate taxes. You do through the Internal Revenue Service right now. If you cannot resist the temptation to put additional taxes burden on the oil and gas industry, if you feel looking at the figures there that the present taxes are insufficient, then let it be on their profits that you determine to be excessive.

You asked my definition of excessive. You and I probably have some difference there. I think they are excessive already.

Senator WALLOP. The profits or taxes?

Mr. MORTON. The taxes are what are excessive, obviously. You are 40 percent partners in the profit of the industry right now. And that seems to be an excessive burden to me. But you have the mechanism for determining profit without any new legislation.

Senator BAUCUS. One question I had, too. I don't know that this is your statement.

Mr. True, look at your table near the end. You go through the windfall profits tax, what the end position and effect ought to be. And your bottom line comes out to say, without windfall profits on the independents, with the applications of 70-percent Federal income tax, it's about 23 cents, with the 50-percent windfall profits tax, it's about 18 cents.

Does the 70-percent income tax rate with you apply? I guess my question is: How much of Wyoming's independents' income is in the 70-percent bracket? It looks like that's how you arrive at the figure 23 cents, roughly.

Mr. TRUE. That is correct. And I have revised those figures because I have never been able to understand where the bottom line in that table comes from. That was lifted from the administration's. I have never been able to anticipate receiving that in our case.

The 70-percent tax is high. Assuming that the additional income retained by the producer is all profit, a good many producers that are in a sizable operation would pay that.

Senator BAUCUS. I am curious. I know it's not fair to average.

Senator WALLOP. That's the administration's table.

Senator BAUCUS. The point is: It looks like it's the basis for earlier statements, say, 19, 20 cents.

Senator WALLOP. Isn't that fair to say that's where other people have been making the case that the plowback already exists? You wouldn't be subject to 70 percent if you were in fact reinvesting?

Mr. TRUE. That is correct.

Senator WALLOP. If you quit where you were and didn't put any more money back into that, you would be at 70 percent?

Mr. TRUE. Yes. That is certainly correct.

Senator WALLOP. Just quit the business and held what you owned?

I did have some experience with the so-called excess profits tax of the Korean war. That was at the time when our little company was trying to expand. And we just couldn't come up because at that time, it went up to 91 percent.

Senator BAUCUS. I guess the 70-percent bracket applies to taxable income over $215,000?

Mr. TRUE. That's correct.

Senator BAUCUS. That was my question.

Senator WALLOP. Dave, I want to explore something that was in your testimony, because we were talking about windfall profits and one thing. But other impediments to production is another item that is important to us.

The example in your testimony about the USGS and BLM playing tyrant is a pretty incredible story and $200,000 loss because of conflicting bureaucrats that couldn't get along.

I think the public should know what is going on. And I hope that you document other examples and send them to me in Washington.

Mr. TRUE. For your information, Senator, when we had breakfast with Senator McClure, he asked for that specifically, he and Senator Stevens. And I did document, I think, six cases and sent to both of those Senators.

I will be glad to include you or come up with some more.

Senator WALLOP. Thank you. You mentioned, also, in your prepared statement that there has been a decrease in drilling for natural gas since the passage of the Natural Gas Policy Act. I wonder how much of a decline there is. And expand a little bit on the reasons for the decline.

Mr. TRUE. Well, the last figure I saw was in the 6 months after the Natural Gas Act was passed. Drilling nationwide decreased by about 20-percent number of rigs in actual use. It has not been that serious in this country.

However, we have had probably 15 percent more days down with our drilling equipment than we had in the comparable period of last year. I think the uncertainty of price is a big factor. We don't know what the price is going to be. Historically, there is no way to tell.

We think that the threat of a rollback in stripper oil prices is an uncertainty that affects drilling. We think that the Federal Government getting price control of intrastate gas, which was the next to the last free market in the petroleum industry, has an effect, the massive 27 or 29 different prices of natural gas contained in that bill and yet to be properly explained by the FERC.

We think that actually the curve that was mentioned here, where expensces exceeded income, has in many cases actually occurred.

I noticed the figure of the price of drilling has gone up 50 or 60 percent in the last 5 years. It's gone up more than that here.

Let me cite two examples. Our daily labor bill, the man at the drilling rig right now, exceeds what we have got for the whole rig, including fuel, bits, power, labor and operating the rig, 5 years ago.

We bought a year ago a new drilling rig to add to the 11 that we had then. We have three rigs that are bigger. Of course, that would leave eight that are smaller or equal in size.

The depreciation on that one drilling rig runs us more per day than our other 11 combined.

That's what is happening to drilling costs and the curves frankly have just crossed. And we didn't intentionally drill 60 percent more than our income last year. We just got involved in some expensive wells and couldn't quit.

It was just the cost escalated on us, much more than we anticipated.

Senator WALLOP. It's interesting to note, talking about natural gas, that not only the increased regulations but the uncertainty of natural gas as an industrial supply is an uncertainty created by EPA's reluctance to come up with their final rules under the Clean Air Act. The figure in the country is, I think, a 7 percent increase in domestic consumption of our total consumption that is now industrial oils that was other fuels just 3 years ago.

And people are wondering why there is a shortage of diesel and gasoline. That's at least one of the reasons, there is a 7 percent greater demand upon the supply that we have coming in. And that's a decreased supply.

Warren, one of the things that shows me that this so-called windfall profits tax bill was really thrown together in a hurry is that there is the exemption you mentioned in your testimony for the windfall profits tax if the oil producing land is held by a State or political subdivision, providing that the receipts go into a trust fund, however, the exemption applies only if all, I mean, 100 percent of those things are dedicated to educational purposes.

Mr. MORTON. That's not the case in the State of Wyoming.

Senator WALLOP. I was going to point that out and ask if it is equitable to tell the State what to do with its own resources.

Mr. MORTON. The State government is concerned about its intrusion by the Federal Government in what was previously considered to be their own area: the land to be dedicated in the State to what they see fit.

While most of our lands have been dedicated to educational purposes, other State land is dedicated to other purposes.

This touches on the question of severance tax, which you raised earlier. The last analysis I have of the House bill, the House recognized the inequity of taxing the producer for the severance tax which they pay to the State and exempted that from the windfall profits tax but then moved on to say that any new taxes passed by the State's severance tax, they would tax that.

In other words, preempting any additional severance tax authority of the State to the Federal Government.

Senator BAUCUS. New taxes would not be exempted?

Mr. MORTON. That's right, obvious intrusion by the Federal Government to a previously recognized tax sanction for the States.

Senator BAUCUS. One question that bothers me is that if there is no windfall profits tax—no tax at all and if we decontrol—I think we should decontrol the crude price at the wellhead—in effect, because of the market strength of OPEC, that OPEC is setting the world price.

Now, it's what—$20—and who knows what it's going to be several months from now? In spot prices, it could be anything. But still it's quite high, which is to say that it's the OPEC price which is going to determine the world price and the cost to consumers.

And that bears little relation to the replacement costs of what it costs to go out and explore and develop oil. And does that seem right?

If the world were competitive, then I have no problem at all, but it's not competitive. As Senator Wallop said, there is no market price.

Mr. MORTON. There is one nation in the world with zero oil production of its own that has absolutely no dependence upon the OPEC nations whatsoever. That is the nation of South Africa, who had the foresight to see this problem and had to courage to take their coal reserves, which are abundant, and go into a complete synthetic fuel system for the whole nation of South Africa. They are the only nation who can laugh at OPEC today.

We have coal and oil shale on capital basis that exceed that of South Africa. What we don't have is the faith to develop those natural resources.

Senator BAUCUS. What you are saying is all of South Africa doesn't import any oil?

Mr. MORTON. No.

Senator BAUCUS. What is their per barrel cost?

Mr. MORTON. I can't tell you what price you are looking at from synthetic coal or crude oil from oil shale. You are looking at the $25 to $30 per barrel figure which is the ceiling price you are going to have OPEC bumping into.

Where does price competition come in? It comes in when you stop subsidizing the use of natural gas and crude oil at below true prices today, which encourage overconsumption, because they are sold below value, and allow other competing energies to come on at their true value.

The tragedy of the Three-Mile Island—the Nation can ill afford not to develop the nuclear. And that unquestionably set back nuclear development many years, something we cannot afford.

But politically, realistically, it has set us back. Yet, nothing has been done to replace that loss from our fixed power bases.

Senator BAUCUS. Really, is the level of $25 roughly the price at which OPEC begins to bump into competitive price? I ask that because of the additional capital costs one has to pay through energy price increases.

Mr. MORTON. What is the alternative?

Senator BAUCUS. I agree we are in a real problem here, but I look again at the figures applied by Mr. True. If you look at his chart which shows the drilling costs increases that our country is faced with, particularly for independents, there is a dramatic shift in 1973 with OPEC.

I don't know whether that's entirely coincidental or not. Drilling costs have increased on nearly a vertical basis, according to information provided, since 1973.

And the earlier estimates were fuels were competitive at about $25 per barrel. I suspect with additional costs, it would be closer to $30 or $35 a barrel. But maybe that's fine. I don't deny that if we have to do that. I think it would probably be a little higher than $25 a barrel.

Mr. MORTON. I am unaware of any restraint we can put on OPEC. As they met in Geneva, even the most radical of nations proposing price increases were still below that range. And there is an automatic ceiling on synthetic fuels imposed because we have the potential of an abundance in these other sources.

Senator BAUCUS. The problem is, as you stated in your statement, we have been addicted to cheap energy in this country for many, many years.

Mr. MORTON. Some tough decisions have to be made.

Senator WALLOP. Where it's going to get tough—one of the OPEC oil ministers—made the statement in Geneva, about the time the west world begins to find competitive ways of creating synthetic fuels, they would lower the price of oil. And that's when you see if you can quit cold turkey and go on.

Mr. MORTON. That's when your resolve will be tested. We are in the game. We can't get out of the world.

We among most nations do have the fortuitous alternative supply. Nobody in this room back here who are all independent oil producers have anything to do with coal or oil sale, but it is a natural resource which we have banked for years, but they are not worth a damn until they are put out in the refinery and put out in the gasoline tanks.

Senator BAUCUS. How do we get there, because OPEC prices is not the replacement cost generally.

Mr. MORTON. That's the only ball game in town.

Senator BAUCUS. In the meantime, a lot of people are trying to get into the oil shale and all the other alternative sources. That's the reason partly for this so-called profits tax and so-called trust fund, is to share with private enterprise and start developing these.

What do you do in the interim?

Mr. MORTON. You might take the profit the Congress seems to be worried about that the major oil companies are going to accrue from deregulation and see that those are plowed back into alternative energy sources.

There is going to be an awful lot of money involved. If you do that, we in this end are going to need some help. You are going to have a problem with water, impact, you are going to have trouble getting water across the State line, something not easily done.

I'm sure you both have been aware of the water in the Sheridan area that was going into Montana, whether it would or would not go with Texas Eastern Pipeline. So, you appreciate the sensitivity of water there.

Impact in these local communities is very real when you put a major plant there.

There are some positive things I think the Congress could be considering to generate this thing. I don't think you need to get the Federal Government into the business.

Senator BAUCUS. What you are saying is significant plowback?

Mr. MORTON. In this instance, synthetic fuels, yes.

Senator WALLOP. I just hope that we do not fall into the seductive trap of creating a trust fund, because that will become permanent and there will be constituencies that will be impossible to wean. There is going to be a lot of money, a lot more than we are talking about, up into $50 billion very shortly. And people are going to be standing in line to get their fingers, their particular proportion of that. We will never break it.

I hope whatever we do, we find a way of channeling the decisions that are made consciously.

Mr. TRUE. Senator, could I make one comment on your question of how we got into this position?

Senator BAUCUS. I know how we got here. How do we get out of it?

Mr. TRUE. I sat on a panel very similar to this 20 years ago in front of the Senate Finance Committee. Our panel didn't have the number, but we had the scenario of what was going to happen if this country kept on with its anti-oil policy of importation and gas price controls and indirect crude oil price control. This was long before the first peacetime price control on crude oil that President Nixon had proposed.

As I say, we didn't have the number right, but we sure had the scenario right. And I can look up that testimony.

Senator BAUCUS. I'm sure you're right.

Senator WALLOP. Let me ask one last question that Senator Baucus and I are interested in.

You mentioned the 1,000 barrel exemption, but do you see that as a risk of production incentive as you come up to that area that is one hole below that figure?

Mr. MORTON. I'm thinking in terms of private investors whom you are soliciting to bring into the industry and because it takes a tremendous infusion of new capital each year to keep our exploration program going.

I witnessed a fact that any one of the earlier speakers who showed that $33 billion would come in as revenue and expenditures had been $34 billion, there obviously had to be outside money coming in. Those people usually started with zero base. And there are always plenty of fresh fish out there you can talk to.

I don't think that's going to be a restriction. But if you don't have some exemptions for them, they are caught between fixed income and raising prices and will say, "Heck, I can do better than that any place else you want."

You raised a question, Senator of what is the fair return on investment and so forth. I would have answered you this way: National return on investment for the industry is running 14 or 15 percent. They are able to go out and raise new capital on Wall Street through this figure, new underwritings go in and roll into those figures. Those figures are acceptable, but the oil has been running 20 to 30 percent below those type of figures for the last 10 or 15 years.

There is a response for that.

Another question you raised: How much money produces how many barrels of oil?

Nobody has an absolute answer to that. Historically, you can trace dollars invested and oil barrels found. Usually this is the obvious response: the more money you invest, the more oil you are going to find.

The Chase-Manhattan economic section, Chase-Manhattan Bank of New York, does a tremendous study. I find that the IPAA in Washington has the best statistical dollars in and dollars out trend of any of the oil agencies. I recommend them to you.

Mr. TRUE. I would like to add a little bit to that. I think any sort of limitation does in fact put a lid on somebody. Now, our operation provides 650 jobs for Rocky Mountain people. And frankly, 1,000 barrels a day limitation would put a lid on our expansion.

Senator BAUCUS. How much of a lid?

Mr. TRUE. It would make it much less attractive to develop a future barrels than it has a past barrel, because there would be less return.

Senator BAUCUS. I am curious whether there is some way——

Mr. TRUE. If size is bad, we are bad. But we are providing 650 well-paying jobs.

Senator WALLOP. Thank you. We will take a break now and come back at 19 minutes till 12.

AFTERNOON SESSION

Senator WALLOP. We'll get started again. Senator Baucus must leave by 2.

And two of his hoped-for constituents from Montana for some reason are not in attendance.

We would like to combine the next two panels, which would be Mr. Robert L. Mullen, attorney from Casper; Mr. Dave Flitner, president of the Wyoming Farm Bureau; Mr. Don Basko of the Wyoming Oil & Gas Conservation; and Mr. Larry McDonald, executive vice president of the Wyoming Industrial Development Corp.

Senator BAUCUS. I might add, if any of you have any statements you want to make in answer to some of the questions that either Senator Wallop or I have raised in earlier panels, feel free to do so. Feel free to address any of your statements to any of those if you feel so inclined.

Senator WALLOP. I would also state that the hearing of this record will remain open for a month. And if anyone would like to make a written statement who didn't have an opportunity to testify, in particular the two people from the Northern Plains Resources Group and Alternate Energy Resources Organization, those statements and others would be welcomed.

Mr. Mullen is not here. Mr. Flitner, will you proceed?

STATEMENT OF DAVE FLITNER, PRESIDENT, WYOMING FARM BUREAU FEDERATION

Mr. FLITNER. Certainly, Senator Wallop. My name is Dave Flitner. I operate an irrigated farm and raise livestock near Greybull. I am also president of the Wyoming Farm Bureau Federation. It's in that capacity as State Farm Bureau president that I testify today.

The Farm Bureau members in Wyoming appreciate your subcommittee conducting a field study in our State on this important issue.

Incidentally, I believe your staff has on file our complete statement, at which I will at this time summarize only nine points in the interest of time.

Point No. 1, the availability of adequate and reliable supplies of energy is one of the most critical problems facing our Nation.

Agriculture's energy needs are critical to the national economy. If farmers and ranchers are to continue meeting demands for food and fiber, they must have adequate supplies of energy.

Farm Bureau believes that the price of energy supplies should be allowed to move freely in response to supply and demand.

Farm Bureau supports decontrol of oil and natural gas prices as an incentive to encourage exploration and development of new domestic supplies of energy, particularly oil and gas.

We favor Congress creating new incentives which would attract capital from individual investors to encourage exploration and development.

We oppose imposing punitive taxes on the energy industry. We think that the so-called windfall tax proposals will be detrimental to those companies which take the risk, exploring and developing new energy sources, like oil and gas.

We think instead of encouraging greater exploration, such a tax would deter domestic discovery and result in an even greater reliance on the less dependable foreign sources of supplies. That's not in the best interests of this Nation.

Philosophically, Farm Bureau believes that any profit achieved by oil companies is better spent in the private sector for more and new jobs and services rather than it being funneled into the Federal Treasury where it could be another source for the big Federal spenders to waste.

Finally, the Wyoming Farm Bureau recommends that the Congress reject any windfall taxes and instead support incentives like decontrol and create new ones to attract more risk capital, to encourage increased domestic oil exploration and development by domestic companies, like the many independents who operate in Wyoming.

Thank you, gentlemen. This concludes the summary of my statement.

[The prepared statement of Mr. Flitner follows:]

STATEMENT OF THE WYOMING FARM BUREAU FEDERATION

The Wyoming Farm Bureau, a general agricultural organization which is organized in all 23 counties, representing ranchers and farmers who produce every type of agricultural commodity grown in our state.

Farm Bureau believes that the prosperity and welfare of our nation's citizens depend upon the availability of adequate and reliable supplies of energy. This is one of the most critical problems facing our country.

The energy needs of agricultural producers are critical to the national economy. If farmers and ranchers are to continue to meet demands for food and fiber, they must have adequate supplies of energy.

Currently this nation's agricultural industry is one of the most efficient producers. Each farmer and rancher feeds himself and 56 other persons. In addition, agriculture accounted for $28.5 billion in exports for the United States in 1978. This helps offset the hefty purchases of the high-priced OPEC crude oil.

Farm Bureau policy says that the prices of energy supplies should be allowed to move freely in response to supply and demand, except in the case of national emergencies or where public utilities are controlled by regulatory agencies.

Farm Bureau members have also been supportive of deregulation of natural gas and crude oil prices.

Why do Farm Bureau members favor decontrol and support allowing prices of energy supplies to move freely in the market place?

In our opinion, such action will encourage both the development of adequate energy supplies and their distribution on an equitable basis.

For generally the same reasons, Farm Bureau has strong reservations about the so-called "windfall" profits tax being considered by Congress. We view such an excise tax as a deterrent to exploration and development of new domestic oil and gas sources. We think the tax would be counter productive to our nation's need to strive for reduced dependence on foreign sources of crude oil. Instead, we think Congress should provide incentives.

To provide positive incentives leading to increased exploration and development of oil and gas by the free enterprise system, we must also encourage capital investment in the development of domestic energy of all types. To achieve this end, Congress should encourage exploration and development through appropriate incentives and avoid imposing punitive taxes on the energy industry. Also consideration should be given to protecting these enterprises against the risk of price manipulation by foreign energy sources which could stop development.

In our opinion, a windfall profits tax on the discovery of new domestic oil is not in the best interests of our agricultural industry and the U.S.

From the farmers' and ranchers' perspective, there is a clearly defined need for a readily accessible supply of energy to produce food and fiber. We need oil and gas. We, in Wyoming, particularly need diesel fuel and gasoline for our agricultural production. We need the assurance that a stable supply will be there. We should not be continually subjected to the kind of shortages we're currently facing.

How does this nation provide such assurances? Obviously it can't do it with greater dependence on foreign sources. We're witnessing the effects of this problem now! The only way for the United States to have the necessary control is to discover new domestic sources of crude oil. (We readily recognize that this alone won't solve the energy problem. It will take a combination of conservation and development of new renewable sources along with production of new domestic non-renewable sources.)

We don't believe that the so-called windfall profits tax will do anything to encourage investment in the exploration and drilling for new oil. Insead of encouraging the flow of risk capital into this much needed oil exploration and development, investors will look elsewhere. Congress should consider formulating an incentive that will attract such capital from individual investors, not just think of incentives as something big oil companies get! We predict that if such a windfall tax is imposed, then eventually there will be fewer and fewer companies in the business of discovering and developing new domestic oil supplies. That will be devastating to this nation.

Here in Wyoming, we are acquainted with oil exploration and development. We recognize that the majority of such exploration and development is done by the independents, not the major oil companies. However, in some cases these independents are exploring for oil under agreements with major companies.

As we understand the proposed energy tax legislation, these independents would bear the greatest tax burden. If that is the case, such will discourage oil exploration here and in other parts of our nation. That's contrary to what's needed. We must do all we can to encourage increased activity by all oil exploration and development firms in a race to find as much new oil and gas as fast as we can.

Philosophically, Farm Bureau members believe that any profits derived from oil exploration and development would be better spent in the private sector for more and new jobs and services rather than being funneled into the federal treasury where it might be wasted by the federal spenders.

In Wyoming, we have a true appreciation for the complex economic system which is so dependent upon adequate supplies of energy. We need adequate supplies of energy for food and fiber production. The energy industry also needs fuels for its activities. Its people need our food and fiber. All of us are dependent upon the transportation industry to bring in supplies and deliver our products to market. The energy industry also needs transportation. In turn the transportation industry needs the agriculture and energy industries. A detrimental windfall tax on energy resources will adversely affect agriculture as well as the energy and transportation sectors.

Farm Bureau recommends that this subcommittee reject proposals to impose a "windfall tax" on the petroleum industry and instead support incentives like decontrol and create new ones which will attract more risk capital, to encourage exploration and development of new domestic supplies of oil and natural gas. Thank you.

Senator WALLOP. Thank you, Dave.

STATEMENT OF DONALD BASKO, SUPERVISOR OF THE WYOMING OIL & GAS COMMISSION

Mr. BASKO. First of all, I want to apologize for my attire. We are in the midst of moving my office, an onerous task at best.

Senator WALLOP. I was going to say I am jealous.

Mr. BASKO. Gentlemen, my name is Donald Baska, the supervisor of the Wyoming Oil & Gas Conservation Commission for the last 10 years. I have been a close observer of the oil and gas industry for the last 25 years, which included approximately 5 years' industry experience.

My position is one of opposition to the proposed windfall profits tax. I know of no other industries that are experiencing excessive profits that are being scrutinized by Congress for a windfall tax. The day-to-day essentials of living quickly point up a number of industries that appears to be making excessive profits; for instance, banking, real estate, and automotive.

This is my own opinion. And I have attached to the back of my statement a more authoritative source from the Journal of Petroleum Technology, June of 1979, which reflects that return on net worth puts the petroleum industry ninth, behind amusements, airlines, drugs, lumber, trucking, autos, food, and clothing.

Likewise, they are sixth in rank behind amusements, drugs, utilities, lumber, airlines, and then comes petroleum on a profit per dollar of sales.

The oil and gas industry is extremely sensitive to adverse political decisions. I have prepared and keep posted a chart of a number of drilling permits issued by the Wyoming Oil & Gas Conservation Commission. It is easy to see what I am referring to. On pages 3 and 4, the Arab Embargo, for instance, started a cycle of increased drilling in November of 1973. The loss of depletion allowance in January of 1975 caused the number of permits to fall back down to a lower level than what we had previously been experiencing.

The event of the crude oil price rollback in December of 1975 caused another loss in activity. The implementation of NTL-6, which is the notice to lessee by the U.S. Geological Survey, and required additional and extensive paperwork to be filed by operators, likewise caused a fallback in the drilling activity. That became effective in July of 1976.

Carter's energy policy announced in April of 1977 likewise caused a decline in drilling activity.

On the other side of the coin, the oil decontrol that took place in June of 1979 caused a spur in activity going up to 255 permits, which is somewhat of a record.

Wyoming has the potential with the right incentives to help alleviate the energy problem. The overthrust belt of western Wyoming is estimated to contain from 1 billion barrels to in excess of 10 billion barrels, and from 7 trillion cubic feet of gas to 25 trillion cubic feet of gas.

Notice I said it would alleviate. It's not going to solve the problem. I believe the estimates are conservative and realistic.

For instance, the Wyoming portion of the thrust belt alone produced 23,000 barrels in 1976, 462,000 barrels in 1977, 1,745,000 barrels in 1978, and 265,000 in January alone of 1979, which should indicate the extent which that portion of the State is exploding.

Likewise, it produced no gas in 1976, 145,000 MCF's in 1977, 3,500,000 MCF's in 1978, and 1,200,000 in January 1979 in the thrust belt alone. This means that 1979 gas production could easily be in excess of 15,000,000 MCF's.

The Painter Reservoir Field is regarded to have 1,000 feet of pay in the nugget formation and recoverable reserves of 250 million barrels. Whitney Canyon Field in the thrust belt has 4,500 feet of pay with potential reserves of 2 trillion cubic feet of gas from the one field above.

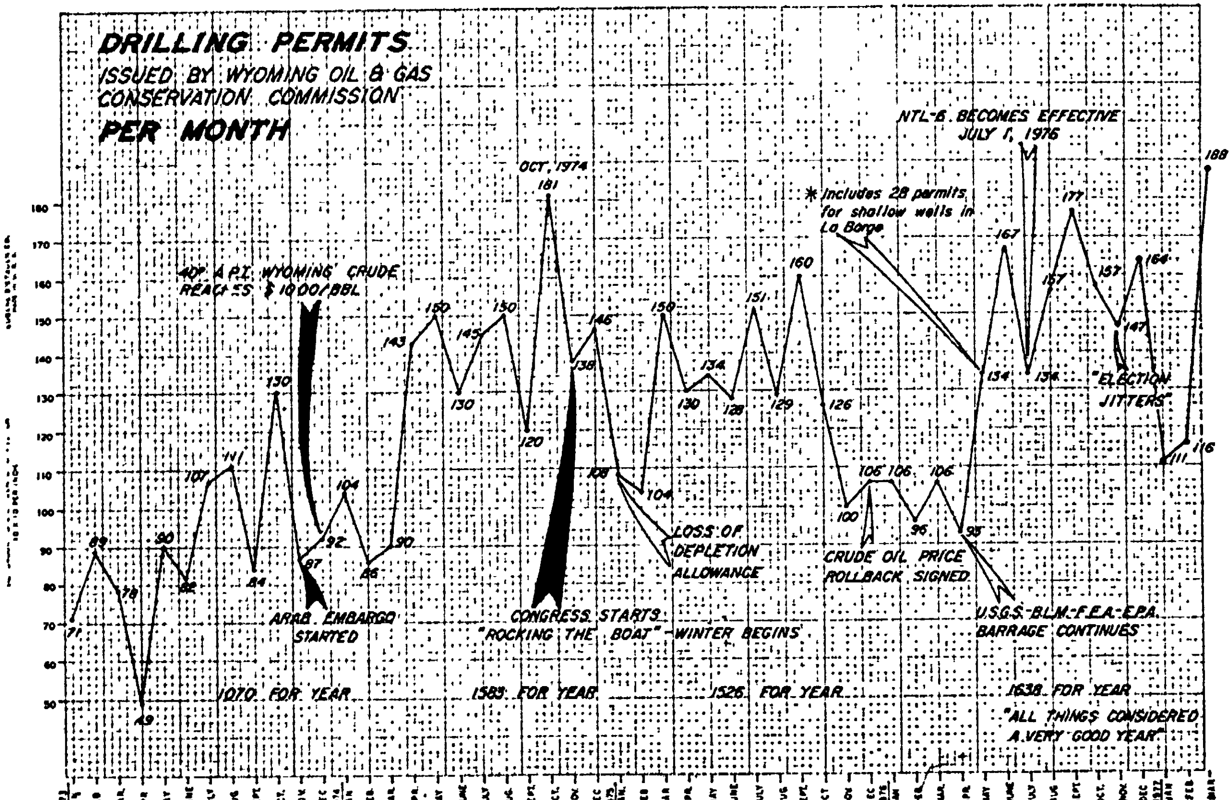
In addition, the thrust belt of Wyoming has literally dozens of untested surface structures with the potential of the fields mentioned above.

Exploratory drilling is extremely expensive and time consuming. A windfall tax would put a damper on the current activity in the thrust belt as well as elsewhere in Wyoming. A tax with a plowback provision would most likely create a bureaucratic morass similar to the Natural Gas Policy Act of 1978—present company excluded.

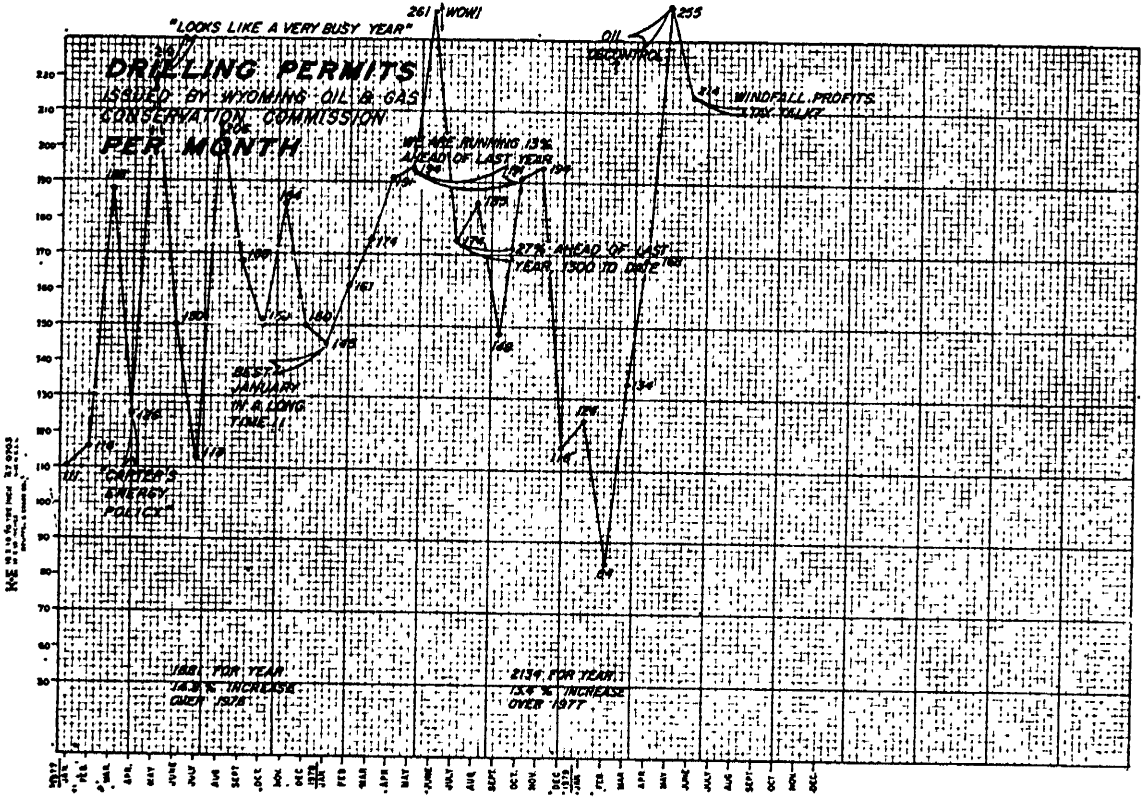
I am intimately familiar with the Natural Gas Policy Act inasmuch as it's our agency that administers the act insofar as the State and fee lands are concerned. And I can tell you gentlemen that 27 separate pricing categories are not easy to deal with.

Thank you.

[The attachments to Mr. Basko's statement follow:]

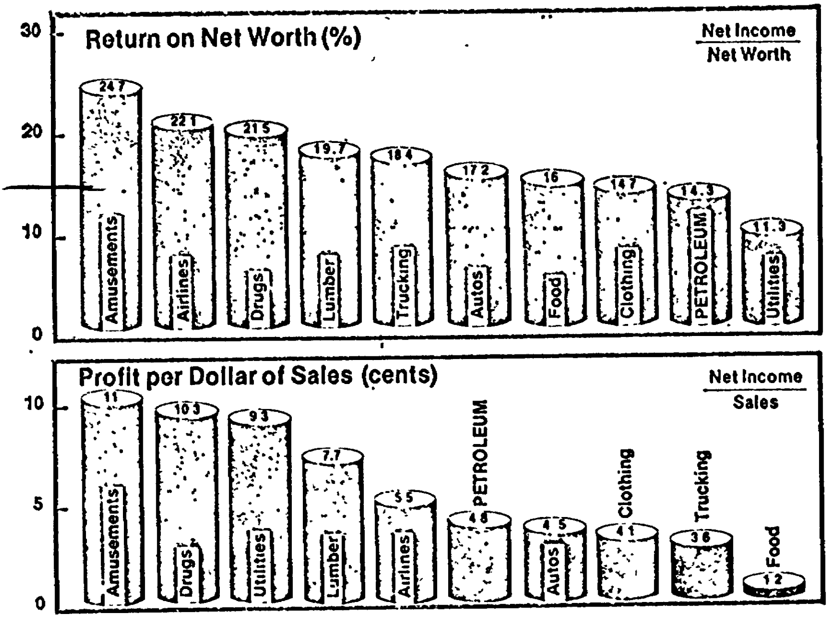


DRILLING PERMITS
ISSUED BY WYOMING OIL & GAS CONSERVATION COMMISSION
PER MONTH
40° A.P.I. WYOMING CRUDE REACHES $10.00/BBL
ARAB EMBARGO STARTED
OCT. 1974
CONGRESS STARTS "ROCKING THE BOAT"
WINTER BEGINS
LOSS OF DEPLETION ALLOWANCE
* Includes 28 permits for shallow wells in La Barge
CRUDE OIL PRICE ROLLBACK SIGNED
NTL-6 BECOMES EFFECTIVE JULY 1, 1976
U.S.G.S.-BLM-F.E.A.-EPA BARRAGE CONTINUES
"ELECTION JITTERS"
1070 FOR YEAR
1583 FOR YEAR
1526 FOR YEAR
1638 FOR YEAR
"ALL THINGS CONSIDERED A VERY GOOD YEAR"


DRILLING PERMITS
ISSUED BY WYOMING OIL & GAS CONSERVATION COMMISSION
PER MONTH
"LOOKS LIKE A VERY BUSY YEAR"
261 WOW!
OIL DECONTROL
255
WINDFALL PROFITS TAX TALK?
WE ARE RUNNING 13% AHEAD OF LAST YEAR
27% AHEAD OF LAST YEAR. 1300 TO DATE
BEST JANUARY IN A LONG TIME!
"CARTER'S ENERGY POLICY"
188 FOR YEAR
14.8% INCREASE OVER 1976
2134 FOR YEAR
13.4% INCREASE OVER 1977

TIC Facts June 1979

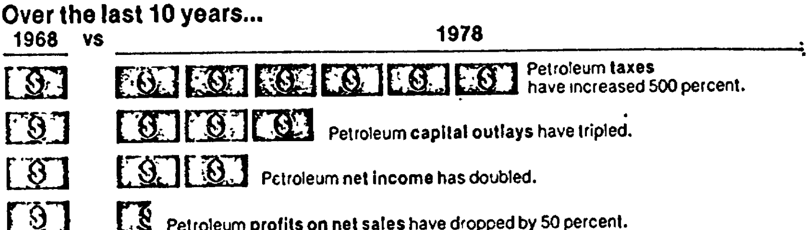
1978 Profits of 10 Consumer Product Industries



1978 petroleum profits were below the national industry averages of ...

- 14.8% in return on net worth
- 5.3% in profit per dollar of sales

Over the last 10 years...



Source Monthly Economic Letter (April 1979) Citibank N.A. NYC Financial Analysis (1978 Preliminary) Chase Manhattan Bank NYC

TIC Facts, a Society of Petroleum Engineers program to promote understanding of the fundamentals of the energy situation, is compiled by a subcommittee of the Technical Information Committee: Granville Dutton, chairman, Bijay S. Banina, Philip C. Crouse, George C. Kunkel, John C. Johnson, Jim Trombta and Cesar A. Lombana.

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Senator WALLOP. Thank you.
Mr. McDonald?

STATEMENT OF LARRY J. McDONALD, EXECUTIVE VICE PRESIDENT, WYOMING INDUSTRIAL DEVELOPMENT CORP.

Mr. McDONALD. Senator Wallop, Senator Baucus, members of the staff, I am pleased to have been asked to appear before this subcommittee. We in Casper are delighted to have the opportunity to comment on energy taxation.

I am Larry McDonald. I have a degree from the University of Denver in finance and economics, and have been employed by the Wyoming Industrial Development Corp. for the past 10 years, serving as executive vice president and chief executive officer for the past 5 years.

Prior to that, I was employed within the oil exploration industry, the last 5 years serving in various capacities with an independent oil well drilling contractor and small oil production company.

While I do not consider myself in any respect an expert on the oil industry, I do have some insight as to how it works.

Wyoming Industrial Development Corp. is basically a nonmineral finance company that finances industrial diversification throughout the State of Wyoming. During my tenure at WIDC, I have studied in depth Wyoming's economy. One such effort was an in-depth economic development study of each of Wyoming's communities which WIDC conducted under a contract with the State's Department of Economic Planning and Development. The study was extensive and took 2 years to prepare.

As an economist, I am deeply concerned with the implications of the proposed energy taxation legislation and, indeed, all Federal regulations and meddling with mineral industries.

Wyoming's economy is very strongly tied to the mineral industry, especially oil and natural gas. While Wyoming's present population is around 400,000, it probably would only be in the range of 75,000 to 100,000 without the mineral industries. Minerals are far and away the most significant economic force in the State.

While coal mining and, to a lesser extent, uranium mining have caught the attention of the press and the public, and rightfully so, oil and gas contribute about 80 percent of Wyoming's mineral wealth. Sales of oil and gas are in the magnitude of $1.5 billion per year. And that would vary some.

We must keep in mind that the oil industry is really five separate industries: exploration; production; transportation, being rail, trucking, and pipelines; refining; and marketing.

Natural gas is like a brand new industry inasmuch as there has not been any exploration specifically for natural gas in over 20 years because of the controlled artificially low price placed on this commodity. With deregulation of natural gas, oil and gas exploration in geologic areas known to contain large amounts of natural gas have dramatically accelerated.

I think as Don has pointed out, that has really been the case in the Overthrust Belt, which for some years has been known to contain gas but got little attention because of the price of the gas.

There are about 150 drilling rigs operating in Wyoming today. And over half are drilling in areas where natural gas potential is great in significance to explorative economics.

Casper economy is almost totally dependent on oil and gas exploration. The population is probably somewhere between 75,000 to 80,000, having grown rapidly for the past 14 years. Annual growth rates have ranged from 3 to 7 percent.

While mining has contributed to Casper's growth, the oil and gas industries, especially exploration-oriented firms, have stimulated this growth. While there are no separate statistics and employment overlaps, employment in exploration probably amounts to 60 percent to 75 percent of Wyoming's total oil and gas industry employment.

I tell people that if they want to know how Casper's economy is doing, read the rig count figures published in the Sunday edition of the Casper Star-Tribune. Historical patterns are interesting.

In 1967, as major oil companies were importing cheap middle-Eastern crude at $1.50 per barrel, Wyoming's rig count was between 30 and 45. Many of these were working on development projects.

In 1968, with the discovery of the Bell Creek field in southeastern Montana, and other significant fields in Wyoming's Powder River Basin, the rig count jumped into the 60's. The Hilite field discovery in 1969 stimulated the rig count to between 90 and 100. With increasingly higher crude oil prices and the decontrol of natural gas, the rig count has steadily climbed to the present 150 rig level.

As an oil and gas service center, Casper is analogous to early-day Denver when it was the mining supply and service center for Cripple Creek, Leadville, Central City and the early Colorado mining communities.

While Casper major oil companies have offices in Casper and control the vast majority of Wyoming's oil and gas production, it is the small operators that explore and discover the majority of the new oil. Something like 95 percent of all wildcat wells drilled are drilled by small independent companies.

In Wyoming there are approximately 350 small independent oil production companies, 200 independent geologists, 100 landmen, 350 oil field service companies and suppliers, 350 attorneys, 200 accountants and many, many other professional people in small companies that depend on the oil and gas industry. The majority of these people operate out of Casper. And the majority of them are small business people.

Whenever Federal taxation and regulations are passed and imposed on the industry, it is these small business people that carry the brunt of the burden. There is a great misconception about the difference between producing oil and earning a profit on oil production. Most of these small oil operators' production comes from marginal or stripper wells.

In a given locality, the cost of exploration, completion, and pumping does not vary substantially from well to well. This is if you've got a variety of wells in the same general area, and if they are about the same depth, the cost of exploring, the dry hole cost, the cost of completing and pumping really runs about the same. It runs about the same whether or not those wells produce 10 barrels a day or you have one that produces 100 barrels a day.

The only real difference—the only major difference, is the amount of income on it. Obviously, the profitability is quite different from well to well.

In any given well, investment decisions are simply a question of matching income from a well with the operating expenses of the well. Once the value of production is lower than the operating expenses, a well is plugged and abandoned, despite the fact that the well could produce additional barrels.

I think you alluded to that in your remarks, Senator.

The cost of regulations affecting the operating expense side of the equation are as fundamental as those of the income or price side. Therefore, stripper well production is especially sensitive to any factors affecting operating income and expenses.

Likewise, when a decision is made to drill in a given location, geologists and engineers can predict what the prospective oil and gas production in a given area might be, if indeed a discovery is made.

Oftentimes, once a wildcast well is drilled and tested, it can be determined that a well would produce some oil or gas, but that it would not produce enough to justify the enormous capital investment costs to complete and operate the well. Potential production problems can be identified and operating expenses predicted.

As a result, many well are plugged and abandoned that would produce some oil, unprofitably.

I would support the political position of subsidizing synthetic oil development, even at costs in the $10 to $20 per barrel range, but some additional oil and natural gas can be produced from wells that are submarginally profitable, if incentives are offered.

It seems rather silly to offer subsidies at these higher prices when some oil increased prices would produce additional oil from some stripper production. It would seem that the proposed tax would be counterproductive in that sense.

A great deal of Wyoming's oil production comes from low production wells and, therefore, any legislation and taxation affecting these wells and independent small business persons involved is critically important to the State of Wyoming, city of Casper, and all of Wyoming's cities and counties.

The State of Wyoming, as well as the State's cities and counties managed and quite responsibly we are leaders in the Nation in financial solvency and our fiscal responsibility. Coupled with good local management, healthy mineral industries provide the majority of the tax revenues to operate our State, cities, and counties.

Casper is not alone in its dependence on the oil industry. Campbell County derives about $33 million per year from property and ad valorem taxes, most of which comes from oil.

I might add, they are able to build their school system, despite the rapid growth problem in Campbell County, basically with oil dollars, and are able to have reasonably low property taxes in that county as a result of oil production.

The Natrona County school system is dependent on almost half of its tax income from one source, the Salt Creek oilfield. Since State government draws the bulk of its income from minerals, the city of Cheyenne, the State capital, is dependent on a healthy industry. Likewise, Laramie is dependent on the University of Wyoming, which is heavily supported by oil industry taxation.

Small communities like Lovell, Greybull, and Upton draw much of their economic dependence from bentonite mining, which is utilized in oil well drilling mud. And nearly every community in Wyoming draws much of it economic independence on oil and gas industries.

While Wyoming has grown rapidly, much publicity has been generated about growth problems. "Mineral impact" became a new catch word. We started talking about the development of the infrastructure. Wyoming has been aggressive in solving its own problems. The Wyoming Community Development Authority was created, State tax funds were reinvested in local communities for schools, water, and sewer systems, urban highways, and an array of physical facilities. We are continuing to help alleviate these impact problems, and build an infrastructure. And we are well along with building the physical plant that it's going to take to get the energy production out of this State.

Governor Herschler has proposed an additional State 5-percent mineral severance tax, and I have no doubt that the measure will eventually pass. While there has been political restraints on the part of many of the citizens of Wyoming not to pass this tax, I think that this resistance would crumble as the public perceives it, as the State is only asking for 5 percent. As they perceive it, the Federal Government is taking 60 percent in the form of a Federal severance tax. I think the Federal Government needs to be more of a leader in physical restraint in this area, if they want to keep every State down to a minimum of taxation.

Revenues, in part, would be utilized to help alleviate growth problems caused by mineral development.

I think the attitude would be that, "Let's get the money while we can. And we need to go build more schools and more this and more of this." And I can see a free for all in taxation for this kind of a bill coming on.

We are indeed concerned about any events, legislative or otherwise, that would weaken the mineral industries in Wyoming, because they are so much an important part of our economy of the State.

Senator WALLOP. Thank you, Mr. McDonald.

I would point out to you that while you have no doubt that the tax will ultimately be passed, the bill as drafted essentially keeps the State from passing that tax. It would no longer be deductible and almost nothing to tax. So, any self-help that the State might be desirous of implementing is simply taken away by the provision that is in front of us, and, at least, has passed the House.

Senator BAUCUS. Unless any of you want to comment on any of the questions I asked earlier panelists—I am still trying to determine in Wyoming and, say, in Montana, what the actual tax is going to be under the President's proposal, because I think it's fair to say that some independents may operate in the 70-percent bracket in some years and not in other years.

I think it's obviously hard to generalize in this area, but if there is some way that we could get some handle on it, it would certainly make it easier for me personally to know the degree to which any of these proposals makes any sense at all.

I do think, as I said earlier, that there will be some kind of a tax. Congress is going to pass some kind of a tax. That being the case, it seems to me to try to fashion one that makes the most sense.

And I am personally better able to answer that question when I have more accurate information. But if you can't now provide that kind of information but can later, I would certainly appreciate it.

Mr. BASKO. Senator, we have a publication that we generate in our office that breaks the production down by operator. And it's arranged with the largest operator first. If you are talking about 70 percent on a given number of barrels, I can provide you with that, if I knew where the cutoff was.

I gather from the comment earlier that it's $215 or some such figure.

Senator BAUCUS. That's under the taxable income.

Mr. BASKO. The magic number. I can't convert that to old and new oil. I can give you the number of barrels all the way down and the percent of the total all the way down to the smallest operator in the State so you could readily see how many small operators it would affect.

Senator WALLOP. You talked about the price being an attraction for the increased development in the Overthrust Belt for natural gas. Let me ask you two questions.

Is that primarily because the gas that is discovered there is new gas and it's fairly easily identified under the price control structure that was there? And the second question is: Has the drilling for natural gas in older fields or proven reserves kept pace with the drilling of the thrust belt, which is new gas and into the complications and the risk that you are going to operate at $5,000 a day without knowing what is going on?

Mr. BASKO. The bulk of the activity of the gas is in three areas, what they call the Wamsutter arch and Moxa arch and the overthrust belt. And all of that is new gas, $2.09 per 1,000.

Senator WALLOP. How are you going with development, well drilling in areas of proven reserves, areas which might come into this strange pricing structure where you are not really certain what price you ought to be able to attain?

Mr. BASKO. It's less attractive, although the price there is $1.98, $1.97, so there is only a 10-cent differential between a new production well and new gas well.

Senator WALLOP. But isn't there a problem that exists, side-by-side structures that still have older prices?

Mr. BASKO. If you drill a well in an older structure and it's identified as a new production well in a field where you are closer than 2½ miles or less than 1,000 feet from an existing well—1,000 feet in depth—they are entitled to new production wells price, which is $1.97. That's what I am saying. There is only a 10-cent differential between that and the new price for rank wildcat.

Senator WALLOP. What happens if you are less than a thousand feet?

Mr. BASKO. That's it. If you are less, it's a new production well. If you are more than 1,000 feet, it's a new discovery, if it's a heretofore unproduced reservoir.

Senator WALLOP. I want to take note of what I think is probably a mistake in the implication in your testimony. My position is one of opposition to the proposed windfall profits tax. I know of no other industry that is experiencing excess profits that are being scrutinized by Congress for a windfall tax.

The implication being that there are excessive profits. I don't think that's what you mean to say, is it?

Mr. BASKO. That's just the terminology. No. I don't view it as excessive. That's just the label that has been put on it.

Senator WALLOP. Dave, I'm interested in your testimony. Does the Farm Bureau's position take into account any worries that individual farmers might have or the bureau of the membership itself of the inflationary effect on decontrol of agriculture production costs?

Mr. FLITNER. About the inflationary effect?

Senator WALLOP. How do you compare that with farming, which is a marginal industry at best and the increased price that would come from decontrol and the inflationary effect on production versus the posture that you would like to have when favoring decontrol?

Mr. FLITNER. I think that's an excellent question, Senator Wallop. I think my answer would be the fact that most agricultural people or certainly most Farm Bureau members are philosophically in favor with bias toward the market system, very strong bias. And certainly the less of two evils in our mind would be to allow the market system to operate and function. And even in the event the price did rise, which inevitably it probably would, the supply would then rise. There is a possibility at some point in time that this would stimulate alternative production, alternative sources and that price would either stabilize or go down.

So, I think our very deep root philosophical feeling is that we would like to stay as close as we can to the market system. We have seen the evidence of Government in every sector of agriculture. And I would say in one word: It is essentially a disaster as it touches each and every one of our operations.

In having said that, I think we are in a gamble. We are in a gamble or crisis at this point that we can't afford very many rabbit trail-type mistakes. Even if there is going to be—and I think there will be—pressure on all of us as individuals and as citizens of this country, we feel that the best solution is to allow the free enterprise system to operate. And even though it's going to be dramatic for all of us in agriculture, particularly, because our margins are extremely thin, if existing, as you said earlier, we feel in the long term this will be in the best interest of agricultural producers and all good people in the United States.

Senator WALLOP. The Farm Bureau and its members are essentially opting for the eventual security of supply rather than worrying about the momentary——

Mr. FLITNER. We are looking at the long-range solution. I think the average producer and average Farm Bureau member would be willing to accept the reality of the transition to where we are if we can get away from the political situation and get a realistic economic solution.

That is really facing the issue that has been addressed by so many gentlemen prior to me this morning, which I happen to agree with most of them. I think this will be resolved.

Senator WALLOP. That brings to mind a question I have, about your testimony where you say you support the political position of subsidizing synthetic oil development, even at costs in the $10 to $20 per barrel range. You know, there has to be an end to that or we get right back in the same circumstance where we are living with subsidized products and begin to use it—and we have grown accustomed in this country to it—so it would never end. I have no problems with subsidizing the startup, but I think there ought to be a clear end in any program we launch on that which would tend to have a subsidy. Would agree with that?

Mr. McDONALD. I definitely agree, Senator. I think we have to remember how the oil shale industry began in 1938, 41 years ago, and is no further ahead today than it was at that time.

Senator WALLOP. That might indicate that some of the other countries in the world have been used to less economic power that is sufficient to buy energy. I think the Brazilians have come up with the technology of producing oil from shale in that country at $13 to $14 per barrel.

Mr. McDONALD. I think synthetic development, in reading the statistics, have always been somewhere from 15 to 17 percent higher than domestic oil production prices. It seems like somehow we have to close that gap so the economics of the system can carry forward.

I would totally agree that you don't solve problems by inflationary methods as this subsidy of synthetics would do, but I do think we urgently need to get with a program of getting it going again.

I haven't given a lot of thought to it myself. Again, we have to remind ourselves we have a strong oil and gas industry in part by the things that were done through taxation, the depletion allowance and so forth, that really created a healthy industry. And perhaps we need to think in terms of finding ways—there are a number that were mentioned today—the plowback method, maybe some tax breaks, rapid depreciation on some of these things, to sort of get the thing going and started up.

Senator WALLOP. What you come back to is what I tried to say in my opening remarks. It isn't the concern of this country about the cost of production. It should be the concern about the cost of replacement, getting in a position where we can deal with those people who have no interest in democracy and no interest in our existence.

Mr. McDONALD. We should not compromise our national security at any price. This is the position I take.

Senator WALLOP. I second it. I guess we already have.

Mr. McDONALD. If it takes $40 oil to protect our national security, in my opinion, that is far more important.

Senator WALLOP. I don't disagree with that.

We want to thank you all. We appreciate your testimony. Again, we may want to ask further questions and have you respond in writing.

Our last panel is Mr. Guy Burton, an independent producer, Mr. Harry Ptasynski, also an independent producer, Mr. Gene George, an independent geologist, Mr. Don Carpenter accompanied by Marv Keller, independent producers and Mr. Tom Showalter, independent producer.

Gentlemen, as you arrive up there, testify in any order you want, just make certain that the reporter knows your name.

STATEMENT OF DON CARPENTER

Mr. CARPENTER. I am Don Carpenter and this is Marv Keller. We are going to indulge in some hindsight at this point that will help the other independents make their remarks about what did happen in our rather limited operation history as a public company.

I am Don Carpenter. I am an independent geologist. I am the immediate past president of the Petroleum Association of Wyoming. Until April 1979, I served as president and chief executive officer of Rainbow Resources, Inc., which was operated as an independent publicly owned oil and gas company from February 1970 through August of 1978.

I anticipated some rather gasps of shock among my colleagues when I identified myself as an independent geologist. I confess to being a little rusty, but I will say that I found over the years that such a title avoids the almost immediate hostilty one experiences when he identifies himself as a corporate president, an oil company executive or indeed simply an oilman.

At the time my small company, Rainbow Resources, was organized, the assets consisted of small interests in oil and gas properties contributed by various founders. Additionally, the company raised $275,000 through a public offering of 550,000 shares at 50 cents a share. This offering closed in February of 1970.

With this minute asset base—and believe me, it is minute in our base—Rainbow Rescurces projected neither/nor a villainous profile in our home territory, the Rocky Mountain region.

In 1972 Rainbow Resources experienced the only incidents in 9 years as a publicly owned independent company of what might be considered a windfall profit.

Because we were small, because we were undercapitalized and we were decidedly the underdog, news of our company's good fortune was widely welcomed and the story of our overnight success had a fairy tale quality, but I will recap the highlights of it: Following an intensive and somewhat discouraging sales effort which was begun in late 1970, the Rainbow staff finally convinced the True Oil Co. of Casper, Wyo., that our Little Mo prospect in McKenzie County, N. Dak., was worth drilling.

A 13,000 foot wildcat was commenced in the spring of 1972 to test the Ordovician Red River formation. Our company retained a one-eighth interest in the oil and gas properties being tested. In July, the Mission Canyon formation of Mississippian age was encountered in an unexpected structurally high position and the well flowed oil when tested.

When word of the oil flow spread throughout the industry, the bazaar sequence of negotiations began. Details of the entire episode are documented in an article by Marvin Keller entitled "Evolution of Redwing Field," published in the August 1973 edition of the Landman magazine.

For these proceedings, let it suffice to say that in the fall of 1972, before the wildcat well reached total depth, Rainbow sold its entire one-eighth interest in the property for $10 million cash, quite a little jump from the $275,000, mostly committed, we had several years earlier.

If this was not a windfall profit, we at Rainbow most certainly regarded it as a providential infusion of capital into our company. I believe this is where it's important.

Tracing Rainbow Resources use of the $10 million is, I believe a good example of how most funds derived from the so-called windfall profits might be employed by other independents.

For openers, we paid the Federal Government and the States of North Dakota and Montana $3½ million in taxes out of the $10 million. This act should have exploded the local classrooms myth that oil companies do not pay taxes but, to my knowledge, it did not.

Next, we addressed ourselves to the question of what to do with our $6,500,000 in change. Should we liquidate our company for approximately $4 to $5 per share, thus giving our original investors 8 to 10 times their money back, or should we continue to explore for oil? We chose the latter.

Rainbow purchased controlling interest in the Medicine Pole Hills Field in Bowman County, N. Dak., for $1,200,000. In those days, we paid $1.25 per barrel for reserves in the ground, which at that time, were selling for $2.80 per barrel.

If you can follow another line of argument we often hear: This would have provided us with a perfect opportunity to simply leave that oil right in the ground that we acquired for $1.25, let the OPEC nations continue to run the price up and reap the windfall profits. Again, however, our decision flew in the face of conventional wisdom and we immediately invested another $2 million improving and upgrading the field production.

From the day we acquired this property to this day, the field has always been produced at a maximum efficient rate. The only interruptions in production have been caused by mechanical problems or severe blizzard conditions otherwise known as windfall snow.

Over the next several years, Rainbow Resources expanded its payroll from 11 to over 40 people situated in Casper, and Denver. During this period, the company initiated many drilling projects in North Dakota, Montana, Wyoming, and Colorado.

In 1974, in another unprecedented action, the company carried out a 1 million acre lease acquisition project in the Williston Basin of Montana and North Dakota. In conjunction with Farmland Industries and a Houston independent, Rainbow began a wildcat drilling program on this acreage which ushered in a period of intense exploration activity, which is still going on to this very day. Our original cost in our share of the leases was approximately $1 million. And we spent much more in subsequent drilling.

As you can tell, for a company that started in 1969 or 1970, actually—by this time, 1976, the game was getting a little bit expensive. Rainbow had paid its bills. By July 1976, we met our bills. We paid our employees. And we were continuing to explore intensively.

At that time the company began drilling the Game Hill unit No. 1-35 in the extreme southern portion of Teton County, Wyo. This well in which we had a 25 percent interest, was set up to test the Frontier formation at 12,500 feet.

The well was located at the eastern edge of the Wyoming Overthrust Belt and was regarded as extremely significant. The projected cost for drilling and completing the well was $1,200,000.

However, during the drilling of the well, several windfall mishaps occurred.

First of all, as we were drilling down, we crossed a thrust fault and the total depth that was necessitated to reach the Frontier formation increased from 12,500 feet to 15,700 feet.

Geological circumstances notwithstanding, two extremely encouraging gas zones were encountered in the well. And a completion attempt was made at this depth, but unfortunately, the 2⅞-inch casing collapsed across the two zones and the chance of an economically rewarded initial well was forever lost.

The well was subsequently completed as a gas producer from a less promising zone. And chances of recovering the original investment seemed remote and will only come about after 70 miles of expensive pipeline is constructed, a project which will take years.

By the way, the well cost over $6 million instead of the projected $1.200,000 By this time, as you can estimate, the $6,500,000 windfall profits were gone with the wind.

And Marvin Keller will pick up at this point and take you on through the deepest and most expensive well ever drilled in the Rocky Mountain industry.

Mr. KELLER. My name is Marvin Keller. I am executive vice president of Rainbow Resources, here in Casper. I would like to direct my comments to the other side of the coin. And that's windfall losses.

The most misused word connected with the current crisis is windfall profits. It seems that any profit made in the oil and gas business is a windfall, while any loss incurred in our business is only the result of ineptness or stupidity on the part of the industry; for example, the huge losses incurred in offshore areas of Florida and the east coast of the United States.

At the present time our company, Rainbow Resources, Inc. is the operator and 23-percent owner of the deepest and probably most expensive exploratory test ever drilled in the Rocky Mountain area.

The No. 1–34 Federal well, located at Pacific Creek in Sublette County, Wyo., has been drilled to a depth of 25.764 feet. And at the present time, we have spent more than $15½ million. We are currently testing the deeper zones to determine if commercial quantities of hydrocarbons are present. Our original primary objectives, the Madison formation has already been tested and proved to be nonproductive.

Because of the extreme depths and expensive well costs involved and the very expensive facilities that would be required to establish production, such as gas plants to remove sulphur, pipelines, and development wells, it is estimated that the total investment would be more than $100 million before any gas could be sold.

If the volume of gas found is not sufficient to justify these kinds of investments, then the entire project will be a failure and none of the nearly $20 million invested will ever be recovered by the owners. Gentlemen, that is a "windfall loss."

Where did this $20 million come from? It came from the past profits of Rainbow and its partners, all of which are independent oil companies. Banks do not loan money to companies to drill exploratory wells and neither does the Federal Government. All of the risk is borne by the companies, but if the venture is successful, any income is suddenly declared "windfall profits."

The costs of exploratory drilling have increased approximately 300 percent since 1973. As the search for oil and gas is expanded to the deeper horizons below 15,000 feet and to remote and geologically complex areas like the Overthrust Belt, the costs of exploration have exploded so that today drilling costs for an exploratory well in the 15,000-foot range may cost from $5 to $10 million.

As a result of this cost squeeze on the companies, their drilling budgets are now being used up very quickly on only a few wells. Today there are many drilling rigs shut down in the Rocky Mountain region, not because the industry is withholding its funds, but because the industry and particularly the independent companies have used up all their available funds.

Think for a minute of how many million barrels of "old oil" have to be produced in order to obtain enough profit to pay for just one new deep exploratory test. Is it any wonder there is a shortage of available funds in the industry?

The only solution is to allow domestic oil and gas prices to rise to world oil prices as soon as possible. The alternative is for America to continue to buy OPEC oil on the spot market at prices up to $40 per barrel.

Who knows? Maybe next year the spot market price will be $60, $80, $100 per barrel. The OPEC countries will continue to raise the prices as long as we are standing in line to buy their oil. It's up to Congress and the President to make the decision.

As a postscript, I might mention that Rainbow Resources was merged with the Williams Companies of Tulsa, Okla., on August 29, 1978. The primary reason for the merger was that Rainbow Resources was not able to continue to finance its widespread exploration activities with its internal oil and gas revenues, which the company was forced to sell at below replacement costs because of Government price controls.

Senator WALLOP. Thank you very much. It's interesting and would be informative if we could get a few of our colleagues to hear the same story.

Tas?

STATEMENT OF HARRY PTASYNSKI

Mr. PTASYNSKI. I am Harry Ptasynski, from Casper, an independent explorationist and oil and gas producer. I hold a degree in geology from Stanford University and have been employed in the oil and gas industry for almost 30 years, 9 years as an exploration geologist for a major oil company and nearly 21 years as an independent consulting geologist and oil and gas producer.

Although I am a director of several oil and gas associations and a member of various professional organizations, I am here to testify against the proposed taxes on domestic crude oil production, the so-called windfall or excess profits tax, as a private citizen who happens to be in the oil business.

In testifying this late in the hearing, it's difficult not to be redundant. I don't care to repeat points that have previously been brought up, but I don't think it would hurt to repeat the importance of the independents in the oil and gas industry.

There are 10,000 to 12,000 individuals and smaller companies comprising the independents who drill most of the exploratory wells in this country.

To refer back to the Overthrust Belt, which has been brought up by the last several people, it might be pointed out that the discovery well of the Overthrust Zone was drilled by an independent company, American Quasar. This is after several major companies had given up fighting the area.

It was also pointed out that the independents derived all their income from sales at the wellhead of oil and gas that they find in this country. We have no foreign production, no downstream operations to supply us with the capital that we need.

And it is also pointed out that the independents historically have vested more than he makes in the oil and gas sales in oil field activities.

In the Bureau of Census annual survey of oil and gas figures in 1973 through 1977, on an average, the independents have reinvested 95 percent of their gross wellhead revenues in exploration and development. Production operations are in excess of that. The production costs have increased markedly.

There are some figures that show that in 1974 there were 623,000 productive oil wells in the United States. To keep these wells in operation or to maintain them, keep them in repair, costs $5.8 billion.

In 1978, there were a total of 655,000 wells. That's a 5 percent increase. Yet, the cost of maintaining these wells went up 55 percent to $8.9 billion. Any excess profit taxes that have been proposed don't take into consideration this type of increase.

Last year the industry spent $16 billion in exploration development and production activity. About half of this was by the independents.

If the country is to make significant reduction in our import of oil from OPEC producers while still maintaining an expanding economy necessary to provide new jobs and investment in the balance of the century, economists calculate that we will have to double our exploration activity. Since the independents conduct the vast majority of these exploratory activities, we are going to have to develop additional capital. And the only possible souice of that capital is increased wellhead price of crude.

We believe the resource base is there.

Although estimates vary, as it has been shown by the testimony of the preceding, leading petroleum geologists estimate that there is as much oil and gas to be found as has been discovered to date. And I would tend to agree with the estimates of at least 100 billion barrels left to be found.

In addition, petroleum engineers further indicate that they can possibly double oil recovery from existing reservoirs in older fields by the introduction of exotic recovery methods. This is additional billions of barrels of oil we are talking about. The oil is there to be found and produced, but it just takes a great amount of capital to find it and bring it up to the surface of the Earth.

The impact of the windfall profits tax—this windfall excess profits tax just drives me up the wall. It's not only a misnomer, I think it's a forensic abuse, but the taxes already take the lion's share of the independent's income. And the proposed excise tax will leave the independent producer with 20 cents if he is lucky.

Senator Baucus, you were curious as to the numbers on the independents who were in the 70-percent bracket. Well, I would like to say one thing, that the independents who are in the 70-percent bracket are the ones who are finding all the oil. And they are the people who should be encouraged.

Senator BAUCUS. Would you break that down, if you could show that?

Mr. PTASYNSKI. They have to be. If you are making $200,000 a year, you are finding some oil and you are successful at it.

Senator BAUCUS. It would be helpful if you could for the record show to what degree those who are in the 70-percent bracket are finding oil. I'm just asking for help.

Mr. PTASYNSKI. Right, but the point I was trying to make, these are the people who are active and who are finding the oil who will be taxed in the 70-percent bracket.

Now, the imposition of an additional tax of whatever size would be, I think punitive and confiscatory and will be nonproductive. Every dollar taken away from the independents is translated into a decrease in domestic production, and increased dependence of foreign oil and the export of dollars and jobs. This current hearing should really be for the consideration of cutting existing producer taxes rather than the possibility of raising them.

The point has been brought up that there has been a drastic decline in domestic drilling activity, which reared its head from October through April. I'm afraid this could become a permanent feature with the imposition of these additional taxes.

The disturbing recent trend of independents selling out their exploration and production facilities is a further disturbing point as exemplified by the Rainbow case, but other cases such as Clarke Oil Refining out of Milwaukee has decided to sell their exploration and producing land because they can't make any money.

Webb Resources in Denver, who was a very aggressive and successful operator, has decided to get out of exploration.

Shenandoah, from Fort Worth, Tex. has liquidated because they looked down the road and saw they couldn't make any money.

This is a very dangerous trend, if it continues. It will lessen competition and increasing concentration in the industry.

With the loss or demise of independent wildcatters, how could we replace his creativity, innovativeness and varied approach that can find oil? To find the most oil is really found when you have the most people looking for it and the most people with different ideas.

Senator WALLOP. Isn't it also true he is likely to take risks that a corporate board wouldn't take?

Mr. PTASYNSKI. Absolutely. He is more flexible, right. Right, Senator.

So, I think it boils down to what the country wants, more energy or more taxes.

I just recently came back just Saturday morning after spending a night in O'Hara from a week's trip in Connecticut. And I had my first experience waiting in line. It was only about 25 minutes.

There was a sense of panic, because I was trying to beat the 6 o'clock closing.

Senator WALLOP. A joyful experience.

Mr. PTASYNSKI. It really is. While I was waiting in line, I talked with the people in front of me. They weren't concerned about the price of oil, just about the availability of it. Windfall profits didn't occur to them. They just want to know when this oil shortage is going to occur.

Now, there is one thing that disturbs me. Senator Baucus made the remark it looks like we are going to have this windfall profits tax or something along that line, that the Congress is going to pass the windfall profits tax.

In the face of all the evidence that has been presented against it, all the cans of worms that this windfall profits tax can open, the difficulty of administration, things of this nature—I don't know why it has to be. Now, 6 months ago, the thought of windfall profits tax was dismissed. There was no chance it would pass Congress.

Six months later when the situation has gotten critical is this clamor coming from somewhere—I don't know from where—for this windfall profits tax.

Senator BAUCUS. Let's face it. There are other Members of the Congress and Senate who are not from producing areas of the country. And I could be wrong. I am just trying to give you an objective sense of the political route.

The Congress is a collection of 535, not 2. It's just my judgment that if you add all 535 together—and most of them come from urban areas, not producing areas—and because of the 2-year House terms, which is the incentive for the quick fix and not to look down the road and find something to make sense—that in all probability, there is going to be some kind of tax. As I said, call it whatever you want to call it. There is going to be some kind of tax.

Mr. PTASYNSKI. It would appear to me they could see far enough into the future to see that the windfall profits tax is not going to result in additional supplies for their constituents. And consumers are the ones that are going to be hurt.

But, be that as it may, if this Government thinks it does need additional taxes—and I don't think it does—but if it thinks it does, I would be in favor of additional tax on the end product, the gasoline, rather than the base source, which is the crude oil.

Such a tax would discourage consumption and would not discourage production. Furthermore, it would be nondiscriminatory and it would apply to foreign produced and refined products and not to just domestically produced substances.

It could also be applied flexibly. For example, it could be exempted or rebated for critical commercial or agriculture or social-type uses.

Failing the substitution of a gasoline or end product tax for an excise tax, I think the independent producer—and I think to the extent of 10,000 barrels per day—should be exempted from this excise tax. There is plenty of precedent for this variation, because many of the existing tax laws variously treat a major company and an independent company.

Now, I am sure all these points and many more will be much more articulately presented to the committee in additional hearings in Washington and possibly elsewhere, but I would like to address one additional point which has to do with the windfall profits tax: that is, the feeling of frustration that constantly faces the industry in general and the independents with limited staffs in particular, in dealings with—they are not dealings—they are just confrontations with the legislative and executive branches of this Government.

We have to spend time fighting seemingly continuous streams of proposals to increase our taxes or impose additional controls and restrictions on us, which increase our costs or proposals to drastically change our ways of doing business, such as leasing procedures, accounting procedures, things of this nature.

And when we aren't fighting this, we are then faced with this army of bureaucrats from the DOE and the EPA and the USGS and BLM and IRS and you name it who are trying to impose on the industry and on us their perverted ideas or interpretation of laws that are so broadly based that you can interpret them any way you want to or so complex that they defy comprehension.

We have to spend this time fighting or we would just be blown off by the seams. I don't know. Maybe some people get a kick out of this type of operation. I think most of the fellows sitting here at this table would rather be in their office or out in the field with their maps and well logs trying to make a buck by finding some more oil. I think this country would be better served in this regard, too.

Thank you very much.

[The prepared statement of Harry Ptasynski follows:]

STATEMENT OF HARRY PTASYNSKI

I am Harry Ptasynski, from Casper, an independent explorationist and oil and gas producer. I hold a degree in Geology from Stanford University and have been employed in the oil and gas industry for almost 30 years—nine years as an exploration geologist for a major oil company and nearly 21 years as an independent consulting geologist and oil and gas producer. Although I am a Director of several oil and gas associations and a member of various professional organizations, I am here to testify against the proposed taxes on domestic crude oil production—the so-called windfall or excess profits tax—as a private citizen, who happens to be in the oil business.

It bears repeating and emphasizing that the independent segment of the petroleum producing industry is at least as important to the energy supply of this country as the more visible and widely known major companies. The 10,000–12,000 individuals and smaller companies comprising the independents drill 90% of all wildcat, or exploratory, wells drilled in this country and find 75% of all the new oil and gas fields. We drill 80% of all development wells and find half of the new reserves. We produce about 40% of the total oil and gas. In contrast with the major oil companies who derive significant amounts of their income from foreign crude production and domestic and foreign pipelines, refining and marketing operations, our only source of income is the sale—at the wellhead—of the oil and gas that we find in the United States. This income, plus money we can borrow on our oil reserves or can promote from outside investors, constitutes the only funds available to us to finance our considerable exploration, development, and production projects. That we are utilizing this income to the hilt is suggested by the Bureau of Census' Annual Survey of Oil and Gas which indicates that for the years 1973–77 independents reinvested 95% of gross wellhead revenues in exploration, development, and production operations.

The industry spent 16 billion dollars last year on these activities—about half by the independents. If this country is to make significant reductions in our imports of oil from OPEC producers while still maintaining an expanding economy necessary to provide new jobs and investment during the balance of this century—a time during which we hope to be making a smooth transition to additional and new energy sources—industry economists calculate that we will have to double exploration and development activity. Since the independents conduct the vast majority of these activities, they're going to have to develop additional capital and the only possible source of that capital is an increased wellhead price of crude.

We believe the resource base is there. Although estimates vary, leading petroleum geologists estimate that there is as much oil and gas to be found as has been discovered to date, and I would tend to agree with the estimates at least 100 billion barrels. Petroleum engineers further indicate that significantly increased oil recoveries from existing reservoirs in older fields are possible with exotic enhanced recovery methods—adding additional billions of barrels. The oil is there to be found and produced—but it will take great amounts of capital.

President Carter's decontrol of crude oil prices—as envisioned by the Energy Policy and Conservation Act of 1975—is a necessary positive step to provide the funds required to make available these vast supplies of additional energy. The increased income resulting from decontrol is, of course, subject to the existing tax laws which already extract the "Lion's Share". The imposition of additional taxes would just about completely negate the positive contributions toward increased domestic supply. The end result could only be the worst of all possible situations: much higher prices to the consumer, no benefit from increased domestic supply (and conversely, an increase in our dependency on OPEC with all its attendant horrible possibilities) and a further bloating of an already tumescent bureaucracy.

The proposed excise tax—the terms windfall profit or excess profit tax are misnomers since the tax bears no relation to profits whatsoever—would fall most heavily on the independents because most of them are unincorporated and subject to the 70% marginal tax rates rather than the much lower corporate. We estimate that out of every dollar of additional income from decontrol, and *without* any additional tax, the typical unincorporated independent will only end up with 21 cents, as shown:

Additional income	$1.00
Average royalties	—.14
Total	.86
State Severance tax	—.05
Total	.81
Additional State & County taxes (Ad valorum, etc.)	—.10
Total	.71
70% Federal Income Tax	—.50
Net to producer	.21

The imposition of an additional tax of whatever size would be punitive and confiscatory, and will be non-productive. Every dollar taken away from the independent is translated into a decrease in domestic production, an increased dependence on foreign oil and the export of dollars and jobs. This current hearing should really be for the consideration of cutting existing producer taxes.

If further taxes are imposed, I'm afraid the drastic decline of domestic drilling rig activity—which plunged 20 percent from October to April—will become a permanent feature. Also, the disturbing recent trend of independents selling out their exploration and production facilities can only continue and expand, thus reducing competition and increasing concentration in the industry. With the demise of the independent wildcatter, how could we replace his creativity, innovativeness and varied approach? The most oil is found when the most people are looking for it in the most places.

What does this country want—more energy or more taxes? If this government thinks it needs additional tax income—and I'm not saying it does—it should impose an additional tax on the end product—gasoline, rather than the source—crude oil. Such a tax would discourage consumption rather than production, would be nondiscriminatory in that it would apply to foreign produced and refined products and not to just domestically produced substances, and could be flexibly imposed—that is, for example, exempted or rebated for critical commercial or agricultural use.

Failing the substitution of a gasoline or end product tax for an excise tax, the independent producer—say to the extent of his producing 10,000 barrels per day—should be exempt from this excise tax. There is precedent for this in the existing varied tax treatment of major company and independent.

Thank you for the opportunity to present my views to this committee.

Senator WALLOP. Thank you.

Mr. Burton?

STATEMENT OF GUY BURTON, VICE PRESIDENT, BURTON & HAWKS, INC.

Mr. BURTON. My name is Guy Burton. I am vice president of Burton and Hawks, a publicly owned small oil and gas exploration company. I represent about 2,500 brave stockholders whom expect us to go out and wildcat for oil. They don't buy 10-cent stock to have us put it in a certificate of deposit in True's interest. They want us to go out and wildcat in the event we might hit something that might be beneficial to their investment.

We own three drilling rigs. And we got into the drilling business as an independent to find oil, not as an independent making money contracting, because it is an arduous job.

We developed one of the rigs just as a wildcatting entity. We search for investors to put up 75 percent of the cost and we put up 25 percent. And we go out and look for oil and gas. We split the benefit of the findings, if any.

The odds against that, of course, are 9 to 1 against finding any oil and gas at all. And the old figure of 45 to 1 was about a 1970 figure, which will be increased now because of increased inflationary looking costs—45 to 1 against finding an economic producer.

Of course, that probably is up to 60 or 70 to 1 on odds against finding an economic producer.

In this realm, we do employ 60 people and one-tenth of True's operations, of course. And if this windfall profits tax is enacted, of course, we will have to stay where we are or get smaller. We can never acquire his status in the industry.

The drilling rig that we use is a small rig, employed to look for oil and gas. It costs $2 million to build. This is a small rig that is capable of reaching 8,000 feet, using all the horsepower available to it. Its workable depth is about 5,000 feet. So, you can see it's not a big rig. That expenditure of $2 million was a big expenditure.

Now, this, of course, demands that this rig be utilized every day. It costs $8,000 a day for this rig to exist. And if it is retarded in exploration efforts by USGS curtailment of activity, while they look for arrowheads or historical sites, then that cost goes on. And we have to absorb those costs.

So, our cost of exploration—Mr. True said that his downtime in regard to the rigs increased every month. And a lot of it is because of the governmental agencies' inability to give us permission to drill on time. We are sitting there with a rig laying next to the lease, waiting for their paperwork to be done.

This is really hurting our exploration efforts, especially in this one rig, fast drilling, fast moving operation, which demands investors, which will leave us if this thing doesn't work.

My question that I would like to ask is that: What are we going to do with the foreign companies that are exploring for oil and gas here in the United States? If you don't know, if you are not aware of it, there are many, many foreign countries now that are investing in oil and gas here in the United States, because this is the last place that you can invest as an individual, or as a government company in finding oil and gas.

We have the French government company that's operating in the Wind River Basin and Williston Basin, Aquitaine.

According to the papers that I read, a government-owned company does not pay taxes. If it's a foreign French government-owned company, which Aquitaine is, they look for oil and gas in our country. They sell the oil and gas. They pay no taxes on that income. If this is true, it's an inequity. That is one reason we are having an influction of foreign companies into this country.

Senator WALLOP. We will look into that.

Senator BAUCUS. That's outrageous. We are in agreement with you.

Mr. BURTON. I got it out of the Christian Science Monitor. And I can reproduce it and send it.

Senator WALLOP. It will be helpful to have that article. We will acquire an answer to it.

Mr. BURTON. It seems to me that Congress—when you people, as part of it, get to Washington, you become rather insulated from the business. And you are here trying to get input. Would it be possible for you to hire a geologist, maybe Don Carpenter, to give you input as to what is happening in the exploration phase of this business?

Senator BAUCUS. If you want to pay more for congressional staff, pay more taxes so the Congress hires more staff—that's the problem. We would all like an expert geologist.

The fact of the matter is, the reservations in Montana, the Tribal Council, want me to hire an Indian, for example. Everybody under the Sun wants me to hire somebody. It's great, I agree. It's a good point.

Mr. BURTON. There doesn't seem to be any experts in that field in Washington.

Senator BAUCUS. I will agree with you on that point.

Senator WALLOP. In the DOE, the primary qualification for membership in that club is that you don't know anything about the production of energy, anything at any level.

Mr. BURTON. That's about all I have to offer, except that I want to be on record as being opposed to any additional taxation on our industry, especially those that put 100 percent of their income back into exploration. And that is inadequate to explore ourselves, so we have to have investors that join us in our efforts. So, anything that would retard our ability to acquire investors, and our ability to put what money we earn into more exploration, those things we are opposed to.

[The prepared statement of Mr. Burton follows:]

STATEMENT OF GUY C. BURTON, VICE PRESIDENT, BURTON/HAWKS, INC.

SUMMARY

(1) Four months for the formation of federal units is excessive.

(2) Delays caused by government agencies are expensive, inflationary and sometimes mortal to the small independent.

(3) In the case cited, personnel of the BLM were inflexible in their work hours (or minutes) to the expense of the applicant.

(4) If the Forest Service representatives of Ashley National Forests are typical, the industry is being blackmailed into unwarranted and unfair expenditures.

(5) The executive branch rhetoric demands an all-out effort by Americans to win the battle against the energy crunch and the various agencies appear to be the enemy.

TEXT

Since I am allowed such a short time for preparing and delivering this testimony I will concentrate on the many frustrating instances of bureaucratic highhandedness that have retarded exploration for, and skyrocketed the cost of, the exploration for oil and gas in one prospect area.

Burton/Hawks, Inc. is typical of many existing small publicly held companies operating in the Rocky Mountain area and the following typifies federally generated exploration delays that threaten their existence.

Geologic indicators of the presence of oil and gas on the southern edge of the Uinta Basin were the impetus for the acquisition of a 60,000 acre checkerboard block by the drilling of 5 wells for a cost exceeding $1.5 million. Besides, the excruciating trauma of having to go through the ridiculous paper work required by the BLM, USGS and Forest Service, we had the problem of raising the capital for the drilling. All this was accomplished and the acerage earned by drilling. Enough shows of oil and gas were found to warrant the formation of federal units to hold the properties by exploration beyond the expiration dates of the leases. This was done at considerable expense and the checkerboard acreage was bought from the owner and resold to raise the capital for drilling the four unit wells to satisfy the USGS unit obligations.

Subsequent events are almost unbelievable and magnify the probability that history will label this decade as the beginning of the era of American self destruction.

To comply with obligations of federal units the applicant must be drilling on the expiration date of the earliest lease in the unit. Drilling earlier or later does not qualify as conforming to the obligations and you lose the unit and all of the encompassed acreage. The drilling bit must be in the ground on the day the lease expires.

Over four months were spent in (1) applying for the units (2) changing the number of acres in the units from 40,000 to 30,000 (3) starting the increasingly complicated environmental reviews and archeological site inspections, etc.

The end of the four month paper battle found the company ready to move the rig on location within just a few days of the fatidic expiration date when we must actually be drilling. The rig and screws cost approximately $8,000 per day mandating an organized and timely rig move. The rig was standing by ready to move when we were informed by the BLM that the bonds should be signed by all working interest owners in the lease (a new one on us). Mr. Bill Hawks flew, at great expense to the Company, a 340 Cessna from Casper to Dallas, Shreveport, Houston, Odessa, and Salt Lake City and arrived with the signed bonds at 4:25 PM. He called the BLM representative, told him of the expense being incurred by waiting to move the rig and that he could deliver the bonds in 10 minutes. Mr. Hawks was told that the closing time was 4:30 and the office would be open to him at 10:00 AM the next morning. The beginning of more frustrating events.

The bonds were delivered, the rig moved toward the location (that had been inspected by four different archeologists representing four government entities) when the Forest Service sent word that we would not be allowed to move on location until we agreed to replace eight existing cattle guards and put in two more in place of gates. They knew that not getting the rig on location would cause the loss of leases on 120,000 acres (187 sections) of land (potentially underlain by 50 billion cubic feet of gas per section). This will cost our company about $30,000 and in the private sector would be regarded as blackmail.

In summary, federally created physical and economic barriers to efficient oil and gas exploration are contributing massively to our inability to decrease our dependency on foreign oil and gas, not to mention the skyrocketing costs of replacing the oil and gas we are consuming today.

Senator WALLOP. I guess if foreign national companies are operating here, it's probably because even with the windfall threat, it's probably more secure than trying to operate elsewhere.

Mr. KELLER. That's not a hell of a choice.

Senator WALLOP. Apparently someone is learning from Iran.

Senator BAUCUS. There is another reason why I think there is going to be some kind of tax. In fact, Senator Long made the statement that he thinks Congress is going to enact some kind of tax. His point is—and I think it's very correct—that if Congress doesn't, the President probably will revoke decontrol. He is able to do that now for a period of time, for at least a couple of years, anyway. That's the main reason why the Congress is probably going to enact some kind of windfall profits tax.

Let's assume the President's tax proposal just for the sake of starting some place. What is the net result to the independent? Is it more revenue? Can it be less revenue?

Mr. BURTON. Decontrol would probably cause a sharp rise in revenue and then a decrease to the point probably below what it is now.

Senator WALLOP. Initially, there would be a lot of things like what Rainbow's study covered, but then as they started pouring it back into the ground, it would probably decrease?

Mr. BURTON. There would be much more drilling if we had decontrol.

Senator WALLOP. I think Senator Baucus's point is what happens if we don't have a windfall profits tax and the President is back on his plan to decontrol? Will you end up with more money or less money?

Mr. BURTON. We have more money.

Senator BAUCUS. We are assuming no decontrol.

Mr. BURTON. Oh.

Senator WALLOP. That becomes one of the unattractive postures we have.

Senator BAUCUS. Assuming the option is, on the one hand, decontrol plus the President's tax—that's the one option. The other is no decontrol, no windfall profit. Which is the better alternative?

Mr. BURTON. I will have to ask my colleagues to help me.

Mr. KELLER. You can go broke both ways.

Senator BAUCUS. Under which alternative do you go broke less quickly?

Mr. KELLER. It's just probably a matter of months.

Senator BAUCUS. Realistically.

Mr. CARPENTER. Honestly, there could be less money available for exploration with a windfall profits tax than a continued control.

Senator WALLOP. I think the Morgan-Stanley piece pretty well indicates that there is no real burden if they were to continue to control and operate on the President's proposal as it was produced and with the House-passed bill, they would probably be better off with continued control.

Mr. PTASYNSKI. Why risk dollar dollars to get 20 cent dollars back if you get something? The odds are against you finding anything.

Mr. BURTON. The controlled prices now—as it is, we are operating and we have been for some time. We are not completely dead. Of course, we are very sick.

STATEMENT OF GENE GEORGE

Mr. GEORGE. My name is Gene George. And I live and office in Casper. And since 1971, I have been an independent geologist. Since 1971, I have been an independent geologist. Since 1978, I have been strictly involved in identifying geologically based prospects for oil and gas-drilling ventures.

I am self-employed. I am probably the smallest of the small independents you will see all day long.

I have a part-time geologic assistant and my wife is my secretary and bookkeeper. I am a certified professional geologist, certificate No. 3347 and am currently president of the Wyoming section of the American Institute of Professional Geologists which issued that certificate in 1976. I believe that my professional integrity is beyond reproach.

You already heard a lot of philosophy today, but I want to tell you about an actual experience that I had a little less than 30 days ago.

I have a half-time retainer with a small-sized independent from Houston, Tex. Under his direction, I developed a geologically based prospect in the Dakota sandstone, which is a known producer in the State of Wyoming. I found good evidence of reservoir development in the Dakota. I identified the trap limits and found shows of oil in the drill cuttings.

Proof of reservoir trap and hydrocarbon by subsurface evidence indicates the presence of a class A drillable prospect. That's about the best evidence you can have for drilling a well.

My client accepted the prospect as first class. The Dakota reservoir will produce 100,000 barrels of oil per well over the life of the field. My prospect has room for 6 wells or 600,000 barrels of oil. A producing field which is of the same type field as my prospect is located just 1½ miles away, which is a direct analogy. The depth to the pay zone in the prospect is only 7,200 feet, which is about the average depth for all wells drilled in the State of Wyoming during 1978.

To add the final positive point, the key lease of 200 acres was available at a reasonable cost.

With all of these encouragements, my client had to turn down the prospect on the basis of unacceptable economics: 100,000 barrels of oil at $13.96 per barrel yields $1,396,000 gross profit; a completed 7,200-foot well costs $325,000. That's a return of $4.29 to 1. The wildcat success ratio for the Powder River Basin in 1978 was 1 in 7. These figures are just the very minimum most people will accept for investment in this type of prospect.

However, in reality, the economics are not so simple. The producer who spends the $325,000 to drill the well also pays up to 20 percent of the $13.96 per barrel as royalty. Now the profit is $1,116,800 with a return of 3.49 to 1 on your money.

Further, if the investment is discounted over the life of the property and if taxes are added, then the return is further diminished to a noneconomic level. Commonly, the drilling money is borrowed at 11 to 14 percent interest or the well is offered on a basis where investors pay one-third of the well cost for one-fourth interest in the production.

In the latter case, the return becomes 2.58 to 1 which is uneconomical.

This is a case where if oil price was allowed to advance with the cost of drilling, the prospect would be profitable. The large oil concerns do not explore for 600,000 barrels of oil because it is not profitable with their overhead. An independent cannot drill for this oil because the cost and risk does not support the return. His investor will not invest at this return rate.

The price of oil cannot be artificially suppressed while the cost of drilling floats with demand and inflation. My 600,000 barrel oil field will not be drilled.

I realize that 600.000 barrels of oil is not a great reserve. I also realize that there is a high risk that the well will be dry and there will be no oil in my prospect. There is a 7 to 1 risk against it.

I feel, however, that my situation is not unique. There are a large number of these types of prospects which will not be drilled under these economics.

And in answer to one of your questions previously, what kind of prices will support activity for these kinds of reserves, I have listed a table here currently at $13.96 barrels, which is Amoco's list price for 38 gravity crude oil—the return is 2.58 to 1. And it's a very, very economic analysis I have done.

I am not in accounting or so forth. I do not have a computer like most of the major companies would run this through.

At $16 a barrel, 2.95 to 1; at $18, 3.32 to 1, which just starts to get at where people will begin to look at this kind of prospect.

At $20 a barrel, it's $3.7 to 1. And you can interest quite a few people.

At $22 a barrel, it's 4.06 to 1. It's then when people start to become interested.

So, you can see just some token increase or even deregulation offset by taxation. If you reduce it back—it wouldn't be difficult to sit here and figure it—if you reduce the profit by some 60 percent, then you get how many dollars it will take to drill my prospect.

If you run it right back down the line—if you take our current $13.96 and take anything off of that, then people won't even talk to me about my prospect.

I don't really have an answer as far as the legislation goes. All I know is I need all of my money invested in my prospects. I do not have a large enough cash flow in my own business to drill a prospect myself. And in order to get a wise investor to invest money in my prospect, even though they may be some of the best well-based documented prospects that I can offer, I have got to have a minimum of a 3 to 1 return on my money for the investor to do that.

Thank you for your time.

Senator WALLOP. Thank you.

Mr. Showalter?

STATEMENT OF TIM SHOWALTER, KIRKWOOD OIL & GAS

Mr. SHOWALTER. My name is Tim Showalter, and I work in Kirkwood Oil & Gas, which is an independent company just based in Casper.

I have a text prepared which you have, so I will just summarize it and not go through the whole text. My point for being here is feeling you need some hard data relating to oil pricing and well costs, et cetera. I would like to present that data.

The summary of my remarks are that I will prepare evidence showing that, due to inflation and drilling costs, we need a significant oil price increase with no additional tax just to keep even with inflation. And to look for new, more risky oil, we will need a price significantly more higher than that. I will provide hard data for drilling costs obtained in Buffalo Field, S. Dak., where Kirkwood has drilled six wells over the past 2-year period.

I refer to a couple tables here for visual presentation. This is the list of wells, the date we drilled the wells, the cost to drill, the percent increased to drill, the price of oil we got for our product, the present increase in oil price in this time period.

We drilled our first well in October 1979. It costs us $425,000. The price of oil was around $12.

On January 1979 we completed our sixth well in the field. It cost us $568,000. The oil price was $13.50. The cost increased to drill the well went up 38 percent. The cost to increase our product we got for drilling that well went up 13 percent.

Our projected wells we are going to start next month ends July 1979 is estimated to cost $605,000. The price will get for our oil is unknown at the present time. Our rig cost increase, figuring $605,000 is a 43-percent increase from the time we started.

If the oil price would rise to meet inflation in this specific field, it would have to reach $17 a barrel just to match inflation over the last two years with no tax.

Senator BAUCUS. What's $17 a barrel——

Mr. SHOWALTER. That's what it would have to be to meet the price of inflation.

Senator BAUCUS. To meet the same rate of inflation increase in cost?

Mr. SHOWALTER. Yes. If the price of oil would increase at the same rate as our drilling costs have increased, it would have to reach $17 a barrel with no increasing taxes.

Senator BAUCUS. What is the revenue you got from the well?

Mr. SHOWALTER. This is the base price.

Senator BAUCUS. Per barrel. How many barrels are you going to get?

Mr. SHOWALTER. Let's go on and maybe I can relate to that question.

Now, we have drilled 6 wells in this field, and we have 10 development prospects that could be drilled. Based on President Carter's classification of oil prices, some of those are on leases that have already produced oil in the past and so they would not be eligible for the new, new pricing and would fall in the upper tier category. Upper tier prices will not increase until January 1980, and gradually be decontrolled to world price by September 1981.

Senator WALLOP. Could you clarify that? Are you saying there was other pay from other zones or other pay from other wells in that area?

Mr. SHOWALTER. No That means that you have a lease, say, that, for example, covers a section of 640 acres of spacing in that area. And that area is 320 acres. So, I drilled a maximum of two wells per section.

We have some leases that cover a section and they have one well on them, but we think there is a reason to drill another well. Under President Carter's guidelines, the price for that oil from that well, if we drill another well on that lease, is not going to increase until January 1980, and gradually rise to the world price in 1981.

The House and also Congress says that increase of price above $13 a barrel would be priced at 70 percent by the House or 60, whatever the number is. And that tax would remain permanent.

We therefore have no incentive to drill those wells. And we never will have. And by the Federal regulations, that oil is being kept in the ground and will not be produced.

Now, how about the category of new, new oil. The new, new oil price is based on property approach. In other words, if you have a lease that has never produced, even if it's close to a field, you can get new, new price. OK.

We have some leases in that area, semiproven, fairly low risk development prospects that would get the new, new price.

Let's look at a table that would show what our rate of return would be. OK. This is a chart of oil prices, percent increase in oil price with no tax, with 50-percent tax and the actual incentive above inflation if the oil prices were raised this month to these figures.

OK. I said the price has to be raised this month for the next well we are going to drill in July to $17 to match the inflation in drilling costs, 43 percent. We have zero new incentive at $17 a barrel from what we have now.

If you raised it to $18 a barrel, the actual price goes up above inflation. We go up 52 percent with no tax, 47 percent with tax. More importantly, the percentage of change relative to new incentive with 50 percent of tax only goes up 5 percent. With no tax, it goes up 10 percent. That's all we are talking about with $18 a barrel. With no tax, it's 10 percent.

Senator WALLOP. Dealing with your $17 figure and 43 with no tax—presumably, your first well has been a profitable well, right?

Mr. SHOWALTER. Yes.

Senator WALLOP. So, there is no real reason to have added incentive over and above that one? Is that right?

Mr. SHOWALTER. OK.

Senator WALLOP. If you get the 43-percent increase and it keeps you level with what is already a profitable well——

Mr. SHOWALTER. Let me cover that in the final statement. I got some comments to sort of try to work this in.

By the way, our rate of return, total rate of return in investment on this well here was 35 percent, on this well, the second well we drilled, with no significant oil price increase and—I'm sorry. This is another column here in rate of return, which I don't have on here, but it was sort of a question you asked.

So, I presented specific data on drilling costs relative to oil pricing and incentives to explore and even develop semiproven reserves. In this specific case of Buffalo Field, Kirkwood Oil & Gas would need a price of $17 a barrel just to match inflation drilling costs with no tax. The price would have to be significantly above that to provide any additional incentive to take the risk to spend our money to drill for oil. And that's what Congress is asking us to do and the President.

Also, due to the classification of oil reserves, some of the oil we think is in the ground we see no reason to try and drill, strictly based on the government regulations and classifications. Some of the oil we think is there that would qualify for a new, new price we may drill, depending on excess profits tax.

Now, relative to your question, this field, I think, is typical of many existing oil fields in the Rocky Mountain area and all over the United States. It suggests that drastic increases in oil prices are needed to find oil with no tax, in cases where you have semiproven wells with fairly low risk, maybe 1 out of 2. The price would have to go much beyond the figures I have talked about to provide a significant new incentive to look in wildcat country.

It's our feeling that the only practical approach for the Federal Government is to remove all price controls with no excessive profits tax. The increase in price will encourage conservation, at the same time, encourage development of new reserves. If any new reserves are developed, the increase in domestic reserves will reduce our dependence on foreign oil and reduce our balance of payments.

Now, before you take the floor with me, I want to respond to one question you asked relative to what happens to reserves if the price goes up to x dollars. OK. And the same questions have been asked: How much oil is there to find?

It's my feeling that forecasting is a complete waste of time. The oil industry and the Federal Government spends millions of dollars predicting what reserves would be found off the east coast of the United States and down the coast of Alaska. And today, no development has been found.

The Thrust Belt has been written off years ago and now significant reserves have been developed. I don't think you can predict.

We have got to follow a philosophy and that philosophy has got to be decontrol, remove all Federal Government control on the oil industry. What you are going to do, you are going to increase incentive. You are going to create jobs in exploring for new oil. You are going to reduce foreign dependence and the balance of payments.

The increased price is going to increase conservation. It's also going to provide direct incentive to people to develop alternate energy resources, which if developed, will eventually get us to the problem of a real supply and demand situation.

In contrast, the Government control gives you a complete negative effect on every one of those things I listed. So, what is the point about arguing how much reserves there are to find? You can't pick a number. Even if you were smart enough to do so, I don't think it would affect your approach if you pick some basic philosophy that is good for the country. Thank you.

[The material submitted by Mr. Showalter follows:]

WILLIAM C. KIRKWOOD,
Casper, Wyo., June 29, 1979.

Re Comparison of Drilling and Completion Expenses Versus Crude Oil Pricing, Buffalo Field, Harding County, S. Dak.

Senator MALCOLM WALLOP,
Senator MIKE GRAVEL
Senate Subcommittee Hearing on Energy Tax Legislation.

DEAR SENATORS: Testimony and written statements at this hearing by Kirkwood Oil and Gas are intended to show that unless oil pricing is completely decontrolled with no excessive profits tax, there will be no incentive to drill and develop new oil reserves. Specific data wil be presented for the Buffalo Field in Harding County, South Dakota to show that an immediate oil price increase to $17.00 a barrel is necessary just to stay even with the inflation of drilling costs over the past two years and that price increase of $20–25 with no excessive profits tax is needed to encourage development of semi-proven oil and gas reserves.

The first well we drilled and completed in Buffalo Field was potentialed on October 3, 1977 with a drilling and completion cost of $425,000. The initial crude price we received was $11.86 per barrel.

The most recent well we have completed in the Buffalo Field was potentialed on January 25, 1979 with a drilling and completion cost of $586,000. The current crude price we are receiving is $13.86. We anticipate starting a new well drilling program in July of 1979 with an anticipated drilling and completion cost per well of $605,000.

One point that is important—all wells in this area are virtually identical in regards to surface equipment, depth, etc. Both wells were drilled and completed with no unusual expenses.

A comparison of drilling and completion costs in the two wells yields an increase from $425,000 to $586,000 or 37.6%. This increase occurred from October 1977 to January 1979. With an anticipated new well cost (May 1979) of $605,000, the price comparison yields a 42.4% increase in drilling and completion costs in 20 months.

Oil revenues have not enjoyed a similar increase. From October 1977 to March 1979, the posted price for 35° API crude in the Buffalo Field has increased from $11.86 per barrel to $13.38 per barrel. A crude oil price comparison indicates a 12.8% increase in crude oil pricing. The 12.8% oil increase is obviously much less than the 42.4% increase in drilling and completion costs.

The time to payout the initial investment on the six wells drilled by Kirkwood in the Buffalo Field ranges from 2½ to 4 years per well. The rate of return on investment for these two wells has decreased from 35% to 25% over the last 20-month period. If oil prices had increased the same rate as drilling and completion costs, the current price for 35° API crude in the Buffalo Field would be approximately $16.88.

In summary, an immediate price increase with no excessive profits tax to $17.00 a barrel is necessary just to stay even with the inflating costs of drilling. To provide significant new incentive to rapidly develop additional reserves in the Buffalo Field, oil prices will have to increase to more than $17.00 per barrel.

Kirkwood has up to 10 development wells to drill in the Buffalo Field. Some of these possible development wells are on properties that have produced oil in 1978 and would not fall under the newly discovered category of President Carter. Under President Carter's new oil pricing regulations, there will be no increase in upper tier price above inflation until January 1980. Upper tier prices will then gradually be decontrolled to world price by September 1981. The House excessive profits bill will tax the difference between the released price and $13.00 a barrel at 70% and the tax will remain permanent. Under the House bill there will never be any incentive to take the risks to develop these semi-proven reserves and this oil will be held from the U.S. market strictly due to complex, useless regulations.

Some of the development prospects are on properties that have not produced oil in 1978 and would qualify for relesed newly discovered oil prices. Under President Carter's oil pricing regulations, newly discovered oil is uncontrolled and can receive the world price. The actual price that will be allowed by President Carter has not been announced. Under the proposed House bill, there would be no tax on the increase in price from the current price to $17.00 and any amount greater than $17.00 will be taxed at 50%, above $26.00 at 70%.

A table has been constructed showing the new increase in incentive to drill for oil and gas in the Buffalo Field with and without a 50% excessive profits tax for oil prices between $17.00 and $26.00 a barrel. With a 50% excessive profits tax, oil prices must increase immediately to $19.00 just to provide a 10% increase in incentive above inflation. If prices go to $26.00 a barrel, the incentive to drill goes up only 39% with a 50% excessive profits tax, compared to 77% with no excessive profits tax.

Data has been presented to compare the cost of drilling to crude oil pricing in a single field in South Dakota. This field would be typical of many oil fields in the United States. The data suggests that oil prices must be increased dramatically with no excessive profits tax to provide incentive to develop semi-proven oil reserves similar to our example in Buffalo Field. The price increase needed to provide new incentive to explore in wildcat areas would be even higher than the development example presented here.

It is our feeling that the only practical approach for the federal government to take is to remove all price controls on oil and establish no excessive profits tax. The increase in price will encourage conservation of energy and at the same time provide incentive to develop new reserves. The increase in domestic reserves will reduce our dependence on foreign oil and reduce our balance of payments.

Respectfully submitted.

William C. Vandeventer,
Registered Petroleum Engineer.
Tim T. Schowalter,
Petroleum Geologist.

50-872—79——7

COMPARISON OF OIL WELL DRILLING AND COMPLETION COSTS VERSUS CRUDE OIL PRICES

Well	Completion date	Drilling and completion costs	Pe cent increase in costs	Crude oil price at completion (per barrel)	Percent increase in crude oil price
11-25 Federal	Oct. 3, 1977	$425,000		$11.86	
12-31 Federal	Jan. 25, 1979	586,000	37.6	13.38	12.8
New well	July 1979	605,000	42.4	(?)	(?)

COMPARISON OF OIL PRICING WITH A 50 PERCENT TAX ON NEWLY DISCOVERED OIL AND WITHOUT

Crude oil (per barrel)	Percent increase in oil price		Increase in incentive as percent of oil costs above inflation if prices were increased as of July 1979	
	With 50 percent tax	No tax	With 50 percent tax	No tax
$17 [1]	43.3	43.3		0.9
18	47.5	51.8	5.1	9.4
19	51.8	60.0	9.4	17.6
20	56 0	68.6	13.4	26 2
21	60.0	77.1	17.6	34.7
22	64.4	85.5	22.0	43 1
23	68.6	94.0	26.2	51.6
24	72.8	102.4	30.4	60.0
25	77.1	110 8	34.7	68.4
26	81.3	119.3	38.9	76.9

[1] Based on House Ways and Means Committee bill passed in June 1979. No tax proposed between current price of approximately $13.50 and $17 oil. Excise profits tax for newly discovered oil is proposed at 50 percent from $17 to $26 oil.

WILLIAM C. KIRKWOOD,
Casper, Wyo., June 7, 1979.

Hon. DICK CHENEY,
Congress of the United States,
House of Representatives,
Washington, D.C.

DEAR MR. CHENEY: Thank you for your letter of May 29, 1979, we approve of your efforts to identify governmental roadblocks to the oil and gas industries attempts to explore federal lands.

We continue to be opposed to changing the current leasing systems as I discussed in our last letter. However, another matter should be investigated at the same time. That matter is the government red tape required to even obtain a permit to drill an oil and gas well. Authority for these permits is with the U.S. Geological Survey and the Bureau of Land Management or Forest Service.

I will briefly try and explain the problems. To drill on a federal lease you have to first get permission to survey the well location. Next you have to write up and design the detail procedures involved in drilling the well. I have included a copy of the paper work required for a well we are trying to permit in South Dakota. Please notice the nit picky response of the U.S.G.S. After the permit to drill paper is sent, an inspection must be planned. At the inspection the operator must have a representative, the rancher must be there if fee surface, a dirt contractor, a U.S.G.S. and a BLM or Forest Service representative. So a minimum of five people must drive to the location and burn up gas merely to make minor modifications in the drilling plans. In no case that I have been involved have these inspections changed significantly the plans of drilling the well or in eliminating any environmental problems. After the inspection the BLM or Forest Service and the U.S.G.S. representatives must finalize the paper work and send a copy to the operator, before he can start work a copy of the plan must be sent to the dirt contractor and be on the location whenever any work is done.

An archeology inspection must also be performed before work can start. If there is snow on the ground an archeologist must be on the location when you start the work to make sure no artifacts are discovered. To my knowledge no significant artifacts have been discovered anywhere on federal lands for the last 3–4 years since this rule has been in effect.

If the well is finally drilled and is then a dry hole the operator must clean up the location and have it inspected again by the U.S.G.S. and BLM or Forest Service.

This whole complex procedure can take anywhere from 30 days to 3–4 months and cost between 2–5,000 dollars per location. The whole procedure serves no useful purpose and costs money and time. The general attitude of the U.S.G.S., Forest Service and BLM is usually negative, slow and uncooperative. Details can be documented if necessary.

To compare, on state or fee lands the procedure is as follows. A one page form must be filled out, no inspection is required. If the well is productive a one page form must be filled out, if a dry hole someone for the state inspects the location, if on fee land the landowner inspects the location.

The ironic thing is there is no consistency with other mineral industries. To explore for coal, uranium or any other minerals on federal land no paper work is required until you are ready to mine. Exploratory drilling for these minerals is analogous to oil and gas drilling and has similar minimal environmental impact.

If you want to take on a worthy cause for the oil and gas industry, removal of federal bureaucratic control on permits to drill should be at the top of the list. All industry groups would be happy to supply tons of information and support. This is a classic case of bureaucratic control that spends taxpayers dollars and slows up industry for no useful purpose except to fatten the federal payroll.

If we can provide additional information please let us know.

Sincerely,

TIM T. SCHOWALTER.

P.S. We have also included a copy of an evaluation of Andrus' ideas on leasing for your evaluation.

Enclosure.

U.S. DEPARTMENT OF THE INTERIOR,
GEOLOGICAL SURVEY,
Newcastle, Wyo., May 18, 1979.

Mr. STAN SPAULDING,
W. C. KIRKWOOD,
Casper, Wyo.

Re W. C. Kirkwood. Well No. 21–23, Federal NE NW Sec. 23-T21N-R3E, Harding County, S. Dak., M-30801.

DEAR MR. SPAULDING: We are returning your application for the above referenced well unapproved. Due to the extreme slopes and anticipated amounts of soils relocation the proposed access road should be "engineered" following the enclosed example.

Several other deficiencies in the APD were also noted at the pre-drill inspection. Those items are listed below and should be corrected prior to resubmission of the APD.

(1) The pad diagram should reflect cuts required at the stake and corrected cuts and fills over the pad.

(2) The landowner forms should be signed and should be site specific i.e., Clarkson should have no input with regards to pad and pit etc.

(3) #2-1 & #2-2 (Planned access roads)—Revise per fileld discussion.

(4) #2-5 Size of culvert should be noted.

(5) #2-7 Gate or cattleguard?—locate same.

(6) #2-8 Roads were *not* staked—this item should be followed in *all* future applications.

(7) #4-1 Facilities not located. Dimensions should be per OSHA regulations and all facilities (pits, etc.) should have dimensions.

(8) #9-2 Revise topsoil stockpile per field determination.

(9) #10-3 Should indicate the reserve pit is to remain fenced until dry.

(10) #11-2 Surface ownership is not Clarkson Land & Livestock.

(11) #11-3 What about the stockpond 300 ft. west?

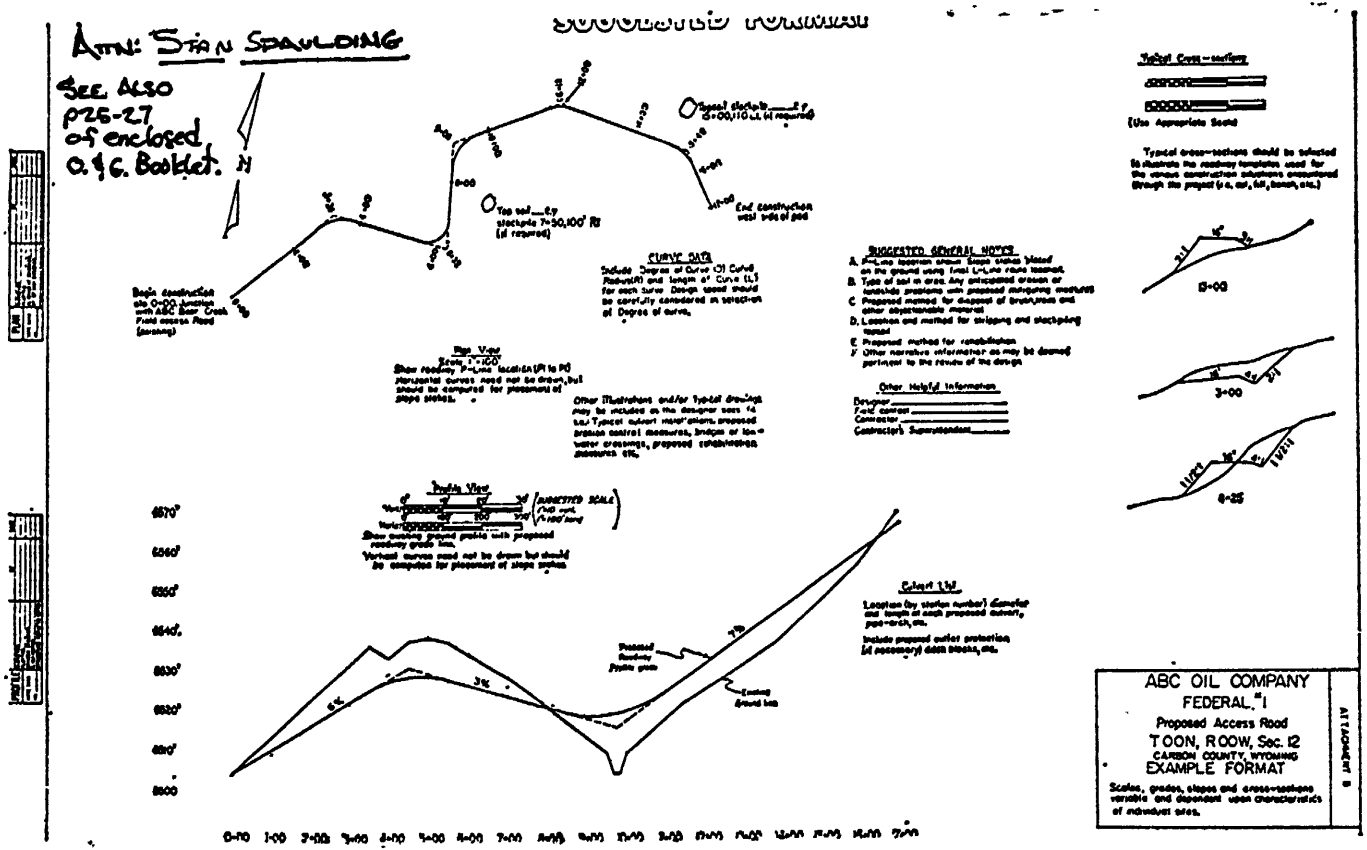
If you have questions don't hesitate to call.

Sincerely yours,

G. E. WORDEN,
District Engineer.

Attn: Stan Spaulding

See also p25-27 of enclosed O.&G. Booklet.



State Pub. Co., Pierre

APPLICATION FOR PERMIT TO:

S. Dak. Oil & Gas Board
FORM 2

[X] DRILL	[ ] DEEPEN	[ ] PLUG BACK	FARM OR LEASE NAME: State
		[ ] SINGLE ZONE	WELL NO.: William C. Kirkwood 33-36 State
[ ] OIL WELL	[ ] GAS WELL	[ ] MULTIPLE ZONE	

OPERATOR: William C. Kirkwood

FIELD AND POOL, OR WILDCAT: Buffalo Field

ADDRESS: P. O. Box 3439, Casper, Wyoming 82602

NO. ACRES IN LEASE: 160 in lease, 320 in drilling unit, E/2 of 3

LOCATION (In feet from an established corner of the legal subdivision): 1980' FEL, 1980' FSL, NW¼SE¼ Sec. 36. T20N, R4E

¼ ¼ SEC. TWP. RGE: NW¼SE¼ Sec. 36 T 20 N, R 4 E

COUNTY: Harding County

NAME AND ADDRESS OF SURFACE OWNER: John H. Niemi, Buffalo, South Dakota 57720

ELEVATION: 3032' GL

PROPOSED DEPTH: 8600'

NO. OF WELLS ETC.: 1

ROTARY OR CABLE TOOLS: Rotary

NAME AND ADDRESS OF CONTRACTOR: Bomac Exploration Company, Suite 700, Westland Bank Building, 10403 West Colfax, Lakewood, Colorado 80215

APPROXIMATE DATE WORK WILL START: August 15, 1979

IF LEASE PURCHASED WITH ANY WELLS DRILLED, FROM WHOM PURCHASED (Name and address)

PROPOSED CASING AND CEMENTING PROGRAM

SIZE OF HOLE	SIZE OF CASING	WEIGHT PER FOOT	NEW OR SECOND HAND	DEPTH	SACKS OF CEMENT
12 1/4"	8 5/8"	24 lb.	New	2000'	Circ. to surface
7 7/8"	5 1/2"	17 & 15.5 lb	New	8600'	1000 sx in two stages.

DESCRIBE PROPOSED OPERATIONS. IF PROPOSAL IS TO DEEPEN OR PLUG BACK, GIVE DATA ON PRESENT PRODUCTIVE ZONE AND PROPOSED NEW PRODUCTIVE ZONE. GIVE BLOW OUT PREVENTER PROGRAM IF ANY

Plan to drill to approximately 2000 ft. and set 8 5/8" surface casing, and circulate cement to the surface. We will install B.O.P. equipment, pressure test and resume drilling to approximately 8600 ft. and if commercial production is encountered, we will set and cement 5 1/2" production casing and complete well.

Spacing unit designated as E/2 of Section 36, T20N, R4E.

MAY 1979
RECEIVED
WESTERN FIELD OFFICE

SIGNED: Stanley H. Spalding TITLE: Operations Manager DATE: May 29, 1979

DO NOT WRITE BELOW THIS LINE

PERMIT NO. ....

CHECKED BY .... School and Public Lands Date

DATE ISSUED / APPROVAL DATE: 6-8-79

Secretary

Supervisor

CONDITIONS:

[ ] COMPLETE SET OF SAMPLES AND CORES IF TAKEN, MUST BE SUBMITTED.

[ ] SAMPLES IF TAKEN, BELOW .... DEPTH, MUST BE SUBMITTED.

SOUTH DAKOTA

Form 9-331 C (May 1963)

SUBMIT IN TRIPLICATE* (Other instructions on reverse side)

Form approved. Budget Bureau No. 42-R1425.

UNITED STATES
DEPARTMENT OF THE INTERIOR
GEOLOGICAL SURVEY

APPLICATION FOR PERMIT TO DRILL, DEEPEN, OR PLUG BACK

1a. TYPE OF WORK: DRILL ☒ DEEPEN ☐ PLUG BACK ☐

b. TYPE OF WELL: OIL WELL ☒ GAS WELL ☐ OTHER SINGLE ZONE ☐ MULTIPLE ZONE ☐

2. NAME OF OPERATOR: William C. Kirkwood, an Individual

3. ADDRESS OF OPERATOR: P.O. Box 3439, Casper, Wyo. 82602

4. LOCATION OF WELL (Report location clearly and in accordance with any State requirements.*) At surface: NE NW 1955' FWL, 785' FNL Sec. 23, T21N, R3E
At proposed prod. zone

5. LEASE DESIGNATION AND SERIAL NO.: M-30801

6. IF INDIAN, ALLOTTEE OR TRIBE NAME:

7. UNIT AGREEMENT NAME:

8. FARM OR LEASE NAME: William C. Kirkwood

9. WELL NO.: 21-23 Federal

10. FIELD AND POOL, OR WILDCAT: Buffalo, Red River

11. SEC., T., R., M., OR BLK. AND SURVEY OR AREA: Sec. 23, T21N, R3E

14. DISTANCE IN MILES AND DIRECTION FROM NEAREST TOWN OR POST OFFICE*: 15 miles NW of Buffalo, South Dakota

12. COUNTY OR PARISH: Harding 13. STATE: S. D.

15. DISTANCE FROM PROPOSED* LOCATION TO NEAREST PROPERTY OR LEASE LINE, FT. (Also to nearest drlg. unit line, if any): 785'

16. NO. OF ACRES IN LEASE: 160

17. NO. OF ACRES ASSIGNED TO THIS WELL: 160

18. DISTANCE FROM PROPOSED LOCATION* TO NEAREST WELL, DRILLING, COMPLETED, OR APPLIED FOR, ON THIS LEASE, FT.: 1950'

19. PROPOSED DEPTH: 8600'

20. ROTARY OR CABLE TOOLS: Rotary

21. ELEVATIONS (Show whether DF, RT, GR, etc.): 3158'GL 3169' KB

22. APPROX. DATE WORK WILL START*: June 1, 1979

23. PROPOSED CASING AND CEMENTING PROGRAM

SIZE OF HOLE	SIZE OF CASING	WEIGHT PER FOOT	SETTING DEPTH	QUANTITY OF CEMENT
12 3/4"	8 5/8"	24#	2000'	~~Circulate to surface~~
7 7/8"	5 1/2"	15.5, 17, 23#	8600'	1000 sx. in two stages

Plan to drill to 2000' and set 8 5/8" surface casing and circulate cement to surface. We will install B.O.P. equipment, pressure test and resume drilling to approximately 8700' and if commercial production is encountered, we will set and cement 5½" production casing and complete well.

Safety Equipment: Refer to 10 Point Safety and Geologic Section

U.S. GEOLOGICAL SURVEY
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APR 4 1979
NEWCASTLE, WYOMING

IN ABOVE SPACE DESCRIBE PROPOSED PROGRAM: If proposal is to deepen or plug back, give data on present productive zone and proposed new productive zone. If proposal is to drill or deepen directionally, give pertinent data on subsurface locations and measured and true vertical depths. Give blowout preventer program, if any.

24.

SIGNED Tim T. Schowalter TITLE Geologist DATE April 2, 1979

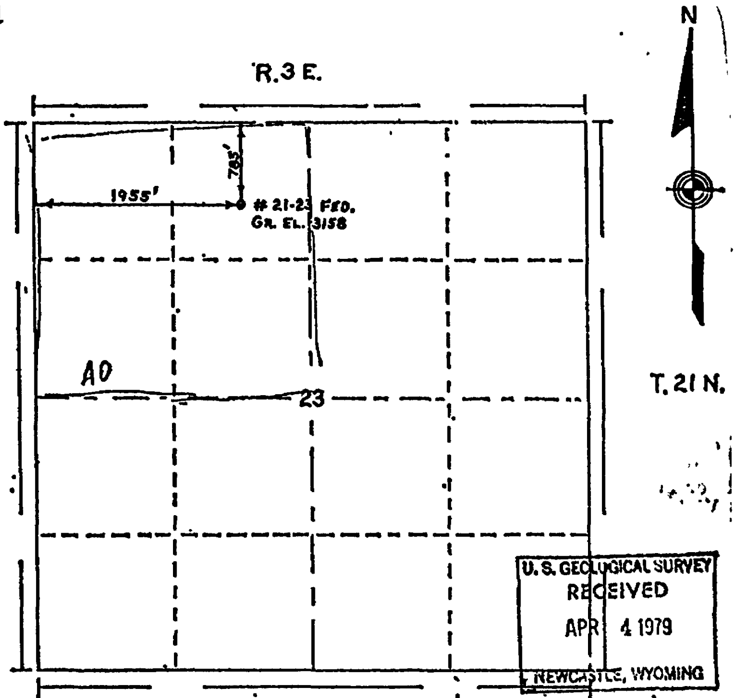
(This space for Federal or State office use)

PERMIT NO. ________ APPROVAL DATE ________

APPROVED BY ________ TITLE ________ DATE ________
CONDITIONS OF APPROVAL, IF ANY:

*See Instructions On Reverse Side

FORM F-105



Scale... 1" = 1000'

Powers Elevation Company, Inc. of Denver, Colorado
has in accordance with a request from TIM SCHOWALTER
for WILLIAM C. KIRKWOOD
determined the location of #21-23 FEDERAL
to be 785' FNL & 1955' FWL Section 23 Township 21 NORTH
Range 3 EAST BLACK HILLS Meridian
HARDING County, So. DAK.

I hereby certify that this plat is an
accurate representation of a correct
survey showing the location of #21-23 FED.

Date: 2/28/79

Gordon L Peterson

Licensed Land Surveyor No 3155
State of So. DAK.

WILLIAM C. KIRKWOOD,
Casper, Wyo.

Re William C. Kirkwood, 21-23 Federal, NE NW Section 23, T21N, R3E, Harding County, S. Dak., M-30801.

GEOLOGIC AND SAFETY EQUIPMENT PROGRAM

1. GEOLOGIC NAME OF SURFACE FORMATION

Hell Creek Formation, Cretaceous.

2. ESTIMATED FORMATION TOPS

	Feet
Dakota	4435
Spearfish	5504
Charles	6643
Soney Mountain	8283
Red River Porosity	8479
T.D	8600

3. ESTIMATED DEPTHS OF WATER, OIL, GAS OR MINERALS

Oil: Oil is anticipated in the Red River Porosity.

Gas: Small quantity is expected in conjunction with oil production in the Red River Porosity.

Water: Ground water is anticipated to approximately 600'. Some brackish water sands could possibly exist below this level, however, the hydrostatic head of the drilling fluid will safely contain these waters within their formation.

Mineral Deposits: No mineral deposits are anticipated to be encountered in this well.

4. PROPOSED CASING PROGRAM

Size	Grade	Weight/feet	Condition	Set depth
8¼ in.	K-55	24	New	2,000 ft.
5½ in.	K-55	15.5, 17 and 23	New	8,600 ft.

5. PRESSURE CONTROL EQUIPMENT

a. Refer to Diagram "A".

b. Minimum pressure ratings on any and all B.O.P. or related control equipment will be 2,000 #/in.

c. B.O.P. Stack will be pressure tested to 500 #/in. prior to drilling out of surface casing. The stack will then be checked on each trip to insure workability.

6. DRILLING FLUIDS

Water will be used as the drilling fluid to approximately 4200' feet and then a non-dispersed, low solids drilling fluid will be used to T.D. No weight material usage is anticipated. Approximately 1500 bbl. of low solids mud will be mixed and approximately 700 bbl. will remain in the hole at completion. The remainder will be allowed to evaporate in the reserve pit and covered during rehabilitation of location.

7. AUXILIARY EQUIPMENT

1. Upper Kelly cock.
2. No floats will be used.
3. Visual monitoring of mud pits.
4. One full opening stabbing valve on floor at all times.

8. EVALUATION PROCEDURES

1. Drill stem tests: To be determined by on site geologist.
2. Coring: None.
3. Logging: IES and Density.

9. ABNORMAL DRILLING CONDITIONS

1. Abnormal Pressure: None Anticipated.
2. Abnormal Temperatures: None Anticipated.
3. Hydrogen Sulfide: None Anticipated.

10. ANTICIPATED STARTING DATE

We anticipate commencing operating by June 1, 1979, or as soon as governmental approval is obtained and rig is available.

WILLIAM C. KIRKWOOD,
Casper, Wyo.

U.S. GEOLOGICAL SURVEY,
P.O. Box 219, Newcastle, Wyo.

Re: Kirkwood 21-23 Federal, NE NW Section 23, T21N, R3E Harding County, S. Dak., M-30801, Point 8, 10 Point Program.

GENTLEMEN: The following acidizing procedures are planned during the completion of the captioned well, as required by point 8 in the 10 point Geologic and Safety Equipment Program.

After perforating and swab testing, 1000 to 3000 gallons of HCL acid will be injected into the perforations. Additives will be added to the acid to clean out mud and sediment from the formation. The acid will be displaced to the perforations with water. Maximum injections pressure will be less than 2000 psi and injection rate 2 BPM or less.

No flammable materals will be injected into the well and no fracturing will be done.

The acid pump trucks will be 125′ from the well head. The acid storage trucks and water trucks will be adjacent to the aci i pump truck.

If there are any questions concerning the outlined procedure, please contact us as soon as possible.

Sincerely yours,

TIM T. SCHOWALTER.

WILLIAM C. KIRKWOOD,
Casper, Wyo.

Re William C. Kirkwood, 21-23 Federal, NE NW Section 23, T21N, R3E, Harding County, S.D., M-30801.

1. EXISTING ROADS

A. Well site staked: Refer to Diagram D and survey plat. All corners and location layout have been staked.

B. Directions to Location: Refer to Map A and Map B.

C. Access Road: Refer to Map B.

D. Existing Roads: (Exploratory) Not applicable.

E. Existing Roads: (Development) Refer to Map A.

F. Existing Road Improvements/Maintenance: No improvements or maintenance is planned on existing road.

2. PLANNED ACCESS ROADS

Refer to Map A for directions to location. Refer to Map B for localized map of area.

1. Width: Road will be constructed as follows: 16-18 ft. in width to allow two-way traffic to location. Raised roadbed 14-16 ft. wide with back sloped ditches will be constructed if well productive.
2. Maximum Grades: Area is in gentle terrain. Maximum grade along access road is less than 8%.
3. Turnouts: (Pull out areas to allow vehicles to meet and pass) None planned.
4. Drainage Design: Natural drainage is to the Northeast from the well site. Appropriate water bars will be made to assure drainage off location and to conform to the natural drainage pattern and to avoid contamination of drainage.

5. Location of Culverts: One culvert will be placed in drainage just east of the location.
6. Surfacing Materials: Native Soil.
7. Gates, Cattleguards or Fence Cuts: Fence cuts will be required and will be gated or cattleguarded.
8. Roads Staked: Roads have been staked into the location with stakes at intervals which allow visual observation from stake to stake.

3. LOCATION OF EXISTING WELLS

Refer to Map B.
1. Water Wells: None Known.
2. Abandoned Wells: Refer to Map A.
3. Temporarily Abandoned Wells: None within 1 mile radius.
4. Disposal Wells: None within 1 mile radius.
5. Drilling Wells: None.
6. Producing Wells: Refer to Map A.
7. Shut In Wells: None.
8. Injection Wells: None within 1 mile radius.
9. Monitoring or Observation Wells: None within 1 mile radius.

4. LOCATION OF EXISTING AND/OR PROPOSED FACILITIES

A. Within 1 mile radius (existing facilities).
1. Tank Batteries: See Map A & B. Tank batteries at each well.
2. Production Facilities: See Map A & B. Production at each well site.
3. Oil Gathering Lines: Koch Pipeline, See Map A & B.
4. Gas Gathering Lines: None.
5. Injection Lines: None.
6. Disposal Lines: None.

B. New Facilities
1. Proposed Location: Refer to Localized Topographic Diagram C. All flow lines will be buried and will be on well site and battery site.
2. Dimensions of Facilities: Refer to Diagram C.
3. Construction Methods and Materials: All construction materials for battery site and pad will be from the site. If productive, gravel from outside the lease area will be used.
4. Protective Measures: The entire battery site as well as the pumping unit will be fenced sheep tight to prevent animal life from entering facilities.

C. Plans for Rehabilitation of Unused Area
All unused and unneeded areas of the battery site and drilling site will be recontoured as is feasible and top soil redistributed for reseeding in accordance with the surface owner and/or B.L.M. within 90 days. Reseeding may be postponed to such time that proper seed germination can be assured.

5. LOCATION AND TYPE OF WATER SUPPLY

A. Location: Produced formation water will be used for drilling. This water will be obtained from producing wells in the area. Specific wells will be provided upon request. Refer to Map A for location of all wells in the immediate area. Heavy salt water will be trucked to location from the Rainbow well near Rhame, North Dakota.
B. Water Transportation: Water will be trucked to our location along existing roads.

C. Not Applicable

6. SOURCE OF CONSTRUCTION MATERIALS

A. Top and sub-soil from road bed and location for construction of necessary roads and location.
B. Construction material is from private surface.
C. See Item A.
D. Not Applicable.

7. METHODS OF HANDLING WASTE DISPOSAL

1. Cuttings: Contained in reserve pit.
2. Drilling Fluids: Will be contained in the reserve pit and allowed to evaporate before being covered with dirt and reseeded.
3. Produced Fluids: (Oil and Water).

No oil will be allowed to escape containment from steel storage tanks. Formation water will be stored in the reserve pit and allowed to evaporate. In the event that oil does accumulate in the reserve pit, it will be removed and properly handled prior to reclamation. Overhead flagging will be installed if oil cannot be promptly and adequately removed.

4. Sewage: The drilling rig will be equipped with a portable toilet with all waste matter being disposed of in the reserve pit. This waste will be chemically neutralized and covered on completion of the well. Sanitary holes will be provided for mobil homes. This sewage will be chemically treated to neutralization.
5. Garbage and Waste Material: A burn pit, approximately 8′ wide, 30′ long and 6′ deep will be dug as shown on the rig layout. This pit will be fenced with small mesh wire to prevent scattering of garbage.
6. Cleanup of Well Site: All debris will be gathered and collected in the trash pit, after the drilling rig has moved out. The location will then be releveled with a bulldozer or maintainer prior to moving in completion rig. Cellar, rathole and mousehole will be filled at this time. Further cleanup procedures are discussed in Item 10.

8. AUXILIARY FACILITIES

Not Applicable

9. WELL SITE LAYOUT

1. Cross Section of Drill Pad: Diagram B shows required cuts and fills. C denotes cuts and F denotes fills. These cuts and fills are surveyed elevations.
2. Refer to Diagram D. No living facilities other than trailers for the toolpusher/supervisory personnel. Top soil will be stockpiled on the northwest end of the location.
3. A preferred parking area is shown on Diagram D. The access road will come into this location from the southeast. The rig orientation is shown in Diagram D.
4. Steel pits will be utilized to circulate drilling mud. The reserve pit will not be lined. However, if soil is too sandy, a coating of bentonite will be applied to prevent excessive water seepage to the surrounding area.

10. PLANS FOR RESTORATION OF SURFACE

1. Upon completion of operations, and if well is to be abandoned, the location will be backfilled, leveled and contoured to as nearly the original topography as is feasible. Any waste material which can be buried without causing environmental damage will be collected and buried in the burn pit. Any other waste will be taken to a sanitary landfill for disposal.
2. The top soil will be evenly spread over the entire location after contouring is complete. The area will then be reseeded. With recommendations from the surface owner and/or B.L.M. The access road will be rehabilitated the same as the location.
3. During the drilling operations the reserve pit will be fenced on three sides. Only the rig side will remain unfenced. The remaining side will be fenced as soon as the rig equipment is moved to allow fencing crews access. This fence will be sheep tight and kept in good repair until R.P. is dry and final cleanup is undertaken.
4. Any oil on the reserve pit will be removed or overhead flagging installed to prevent birds from landing.
5. Ninety days after completion of drilling and completion operations, the surface will be re-contoured in such a manner as to not interfere with production activities. Re-seeding, however will be postponed to such time as germination of seeds can take place.

11. OTHER INFORMATION

1. Topography: Refer to Topographic Map B.

Soil Characteristics: Sand and slightly bentonite.

Geologic Features: No distinguishing geologic features are present.

Flora and Fauna: Area is covered with native grass and sagebrush with migratory wildlife in an area.

2. Surface Use: Land is used only for pasturing livestock.
Surface Ownership: Clarkson Land and Livestock
3. Proximity of Water: Closest reservoirs are approximately ½ mile from location. Intermittent stream drains the area approximately 350 feet east of location.
Occupied dwelling: None.
No archeological, historical or cultural sites are within a two-mile radius.

12. LESSEE OR OPERATORS REPRESENTATIVES

William C. Vandeventer, 300 Market Square, Casper, Wyo. 265-5178.
Tim T. Schowalter, 300 Market Square, Casper, Wyo. 265-5178.
Stanley H. Spalding, 300 Market Square, Casper, Wyo. 265-5178.

13. CERTIFICATION

I hereby certify that persons under my direct supervision have inspected the proposed drill site and access route; that I am familiar with the conditions which presently exist; that the statements made in this plan are, to the best of my knowledge, true and correct; that the dirt work associated with the building of the road, location and battery herein will be constructed by a later named contractor. All contractors and subcontractors will conform with this plan and the terms and conditions under which it is approved.
Date: April 2, 1979.

TIM T. SCHOWALTER,
Geologist.

REHABILITATION AGREEMENT

Lease Number: M-30801
Well Name and Number: 21-23 Federal
Location: NE¼ NW¼ Sec. 23 T. 21 N., R. 3E

William C. Kirkwood, an individual Oil Company intends to drill a well on surface owned by Clarkson Land & Livestock. The lessee/operator agrees to complete the following rehabilitation work if the well is a producer:

[X] Yes [ ] No Maintain access road and provide adequate drainage to road.

[X] Yes [ ] No Reshape and reseed any area in excess of pump and support facilities.

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Other requirements: ______

The following work will be completed when the well is abandoned:

[X] Yes [ ] No Site will require reshaping to conform to existing topography.

[X] Yes [ ] No Pit will be fenced until dry, then filled to conform to topography.

[ ] Yes [ ] No Entire disturbed area will be reseeded. If yes, the following seed mixture will be used:

2# Yellow Sweet clover, 5# Western Wheatgrass
2# Crested Wheatgrass

[X] Yes [ ] No Access road will be rehabilitated and reseeded using the same seed mixture as above.

[ ] Yes [X] No Access road will remain for landowner's use.

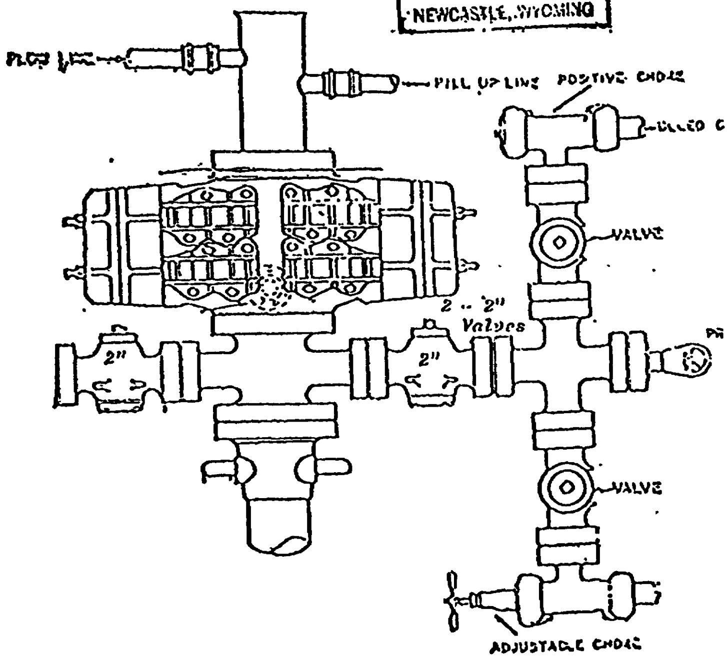
Other requirements: ______

Landowner		Operator/Lessee	
Name:	Clarkson Land & Livestock	Name:	William C. Kirkwood
Address:	c/o Jim Clarkson	Address:	P.O. Drawer 3439
City:	Buffalo	City:	Casper
State:	South Dakota 57720	State:	Wyoming 82602
Telephone:	605 375-3262	Telephone:	307 265-5178
Date:	4/1/79	Date:	4/1/79

[ ] Yes [ ] No I certify rehabilitation has been discussed with the surface owner.

______
Surface Owner's Signature
Jim Clarkson

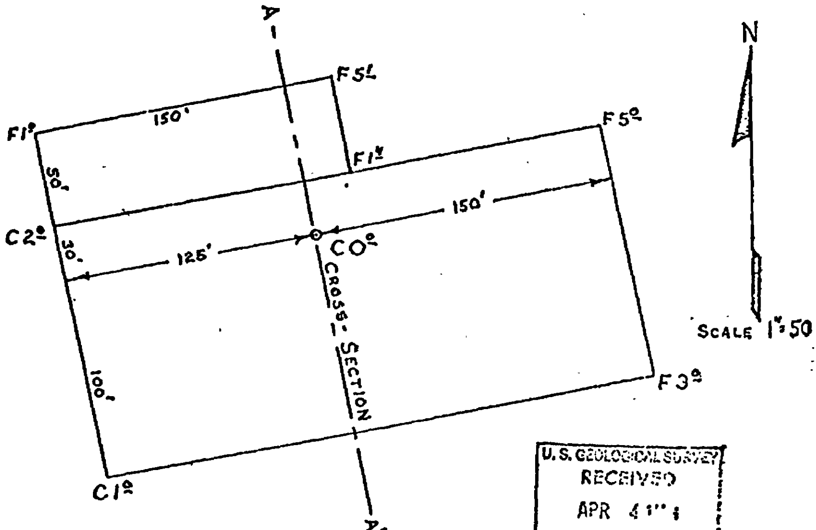
TYPICAL B.O.P. STACK



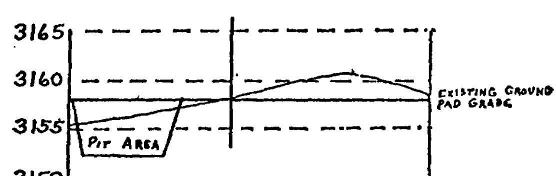
NOTE: - BLOWOUT PREVENTER HAS DOUBLE RAMS; ONE BLIND AND ONE PIPE RAM..

DIAGRAM A

WILLIAM C. KIRKWOOD
21-23 FEDERAL



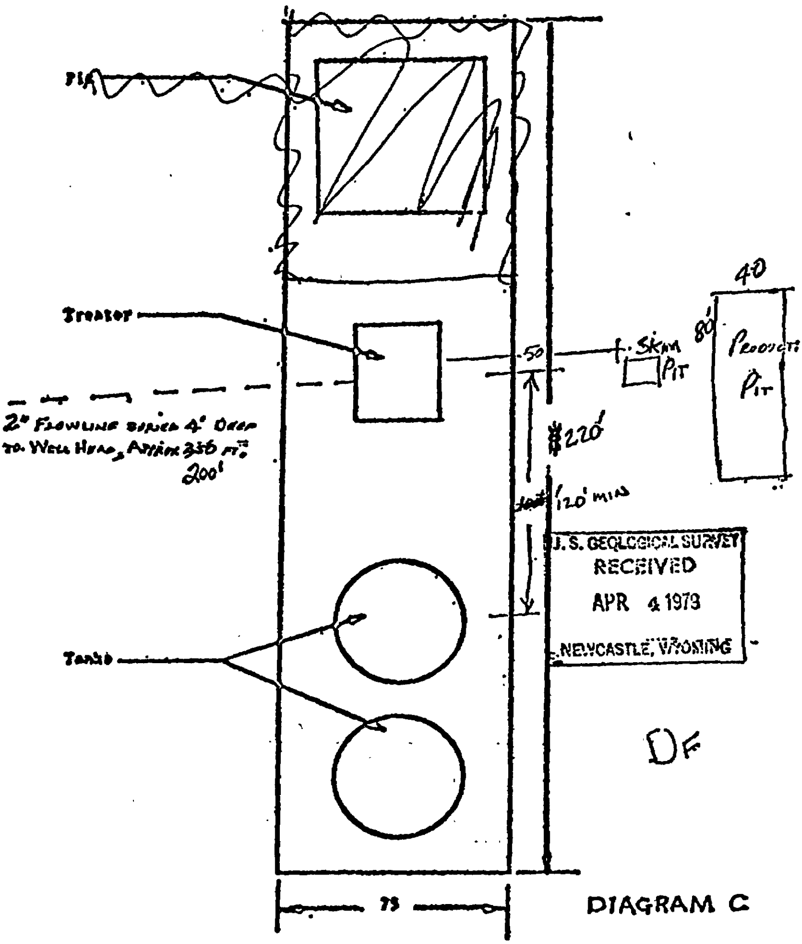
U. S. GEOLOGICAL SURVEY
RECEIVED
APR 4
NEWCASTLE, WYOMING



CROSS - SECTION A TO A'

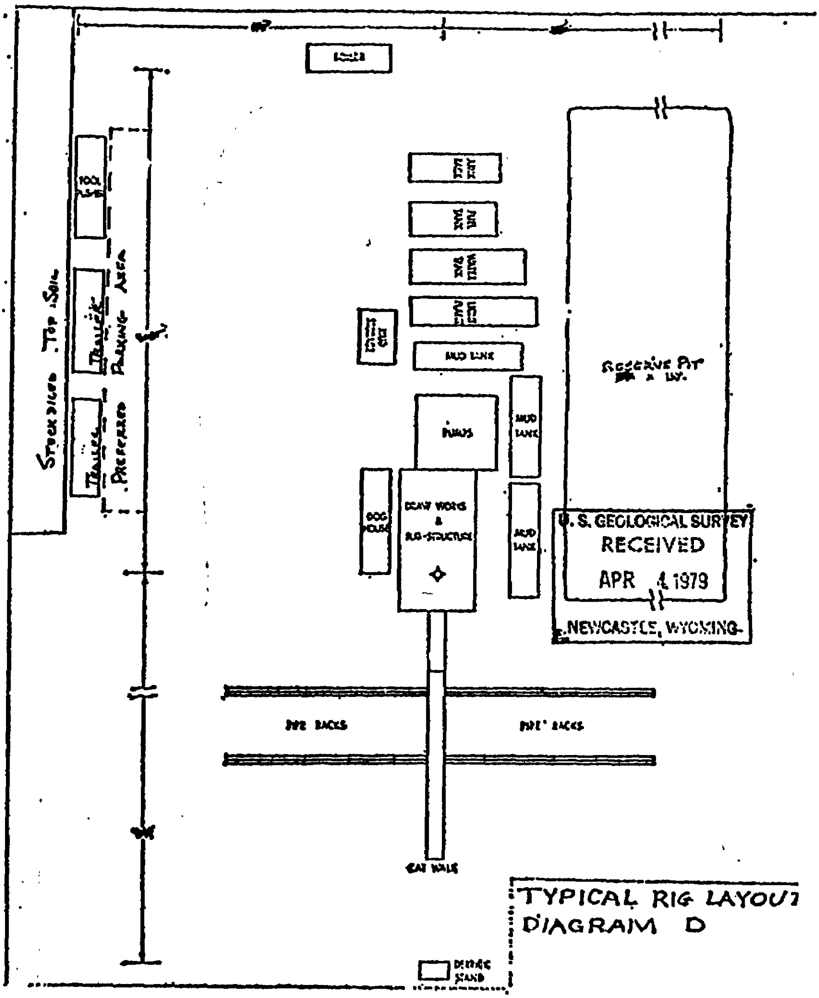
DIAGRAM B

SCALE
HORIZ. 1" = 50'
VERT. 1" = 10'



Pit
Treater
2" Flowline buried 4' deep to Well Head, Approx 350 ft.
200'
Tanks
75
50
Skim Pit
40
80'
Production Pit
220'
120' min
U. S. GEOLOGICAL SURVEY
RECEIVED
APR 4 1973
NEWCASTLE, WYOMING
DF

DIAGRAM C



TOOL SHED
TRAILER
TRAILER
PREFERRED PARKING AREA
STOCKPILED TOP SOIL
MUD TANK
PUMPS
MUD TANK
MUD TANK
DOG HOUSE
DRAW WORKS & SUB-STRUCTURE
PIPE RACKS
PIPE RACKS
CAT WALK
RESERVE PIT
U.S. GEOLOGICAL SURVEY
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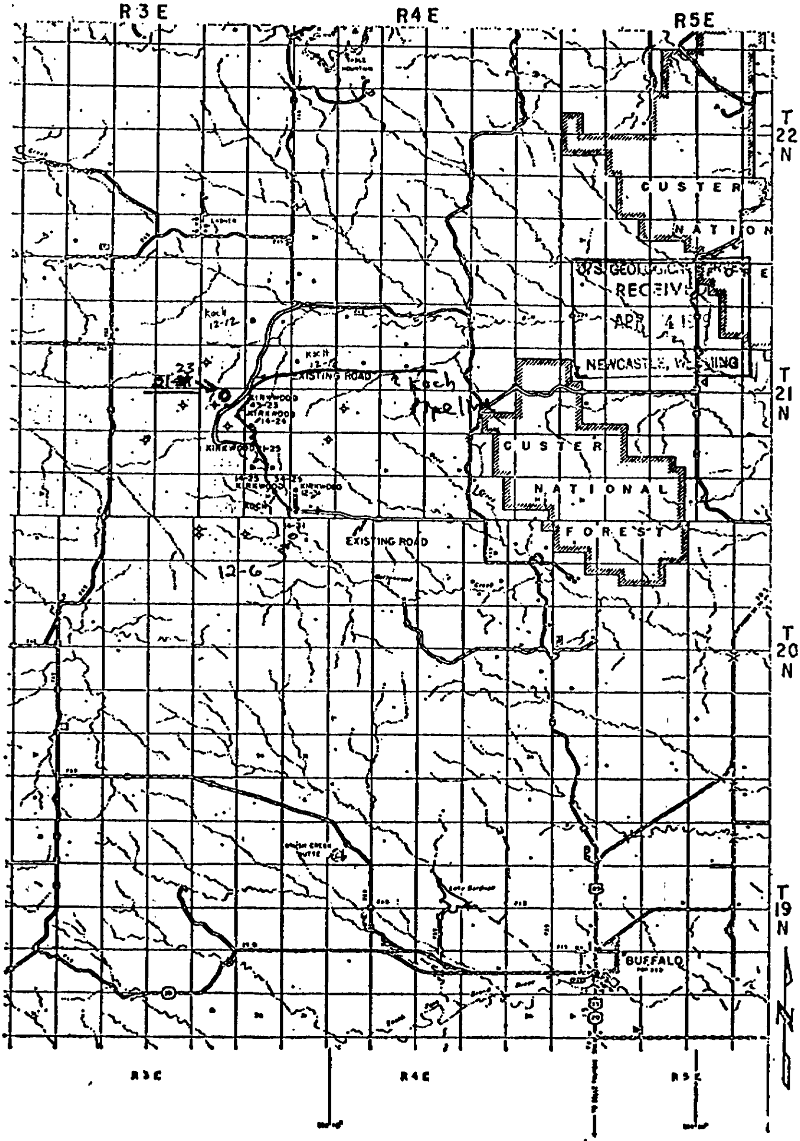
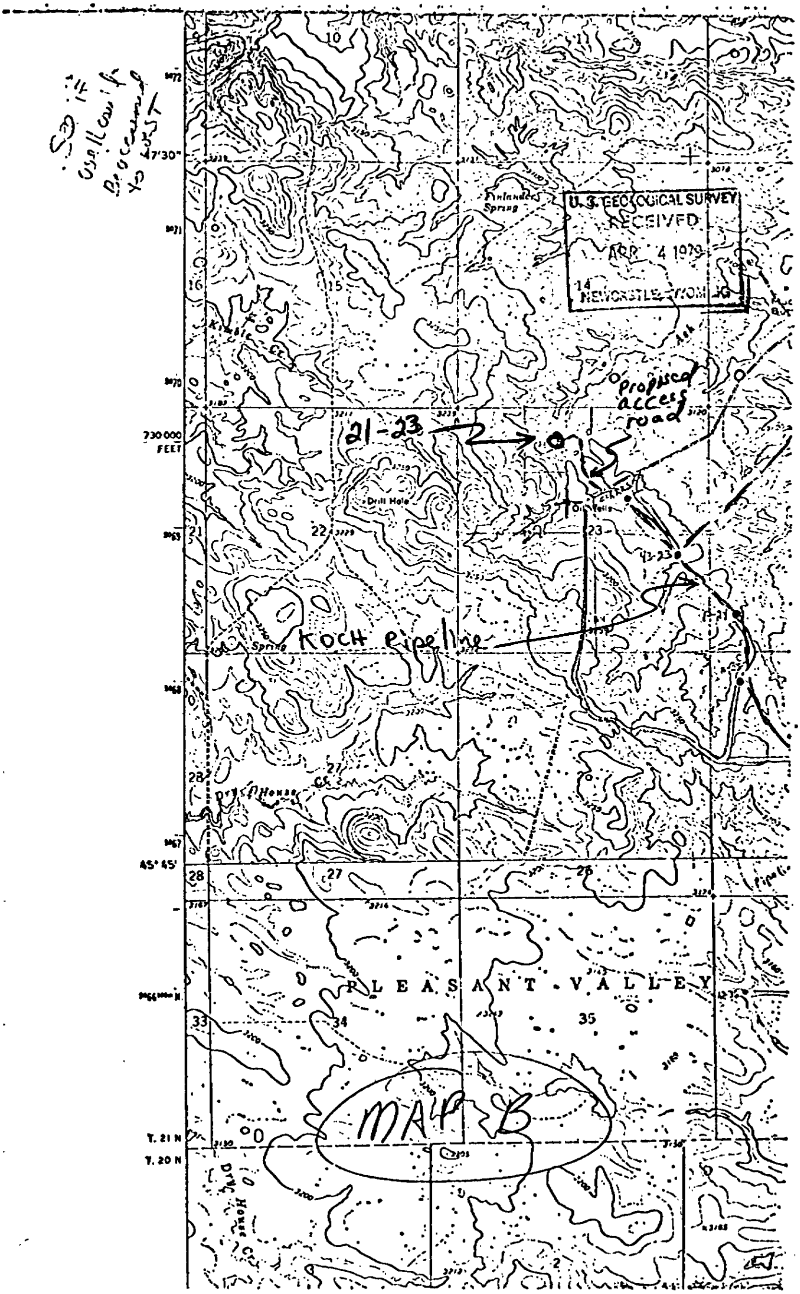
NEWCASTLE, WYOMING
TYPICAL RIG LAYOUT
DIAGRAM D



ROAD LOCATION MAP TO ~~12-26~~ 21-~~24~~ + 12-6

WILLIAM C. KIRKWOOD
P.O. DRAWER 3439
CASPER, WYOMING 82602


Finlanders Spring
U.S. GEOLOGICAL SURVEY
RECEIVED
APR 4 1979
NEWCASTLE, WYOMING
Proposed access road
21-23
Drill Hole
Oil Wells
43-23
KOCH Pipeline
Spring
Kimble Cr
Dry Hollow Cr
PLEASANT VALLEY
MAP B
730 000 FEET
47'30"
45°45'
T. 21 N
T. 20 N
10
16
15
21
22
23
28
27
26
33
34
35
2

Senator WALLOP. I have one question that deals with this whole spectrum of enhanced recovery.

As I understand it, there are all kinds of exotic techniques that get more and more expensive as you go along.

Can you give me or can you give the committee an idea of how expensive it is to take a subsiding field, declining field, engaged in—take an average Wyoming field such as Mr. George described of 7,200 feet. And you want to engage in tertiary recovery. How expensive is that and how long could you expect to prolong the life of the field on just an average basis?

I know you are talking about different ones in different fields. Is there an answer to that?

Mr. KELLER. I'm not an engineer. I can start off on this thing a little bit. Normally, they figure 10 to 20 percent of the oil is recovered on primary, depending on the type of reservoir in the field.

That means there is anywhere between 80 and 90 percent still in the ground. That's in any field. Now, a normal secondary water flood that they use, which is a fairly simple proven way of increasing production, generally doubles where these prove feasible to operate—will double your primary production.

Then you are looking at 70 to 80 percent of the oil.

Senator WALLOP. What does that do to the cost of production?

Mr. KELLER. It gets expensive.

Senator BAUCUS. How much more expensive is it?

Mr. KELLER. I don't have a dollar figure. Probably somebody back here could come up with something.

Mr. KEATING. Bell Creek Oil Field in Gary Operating is doing a polymorph detergent tertiary program in that field. And the cost of producing a barrel of oil in the tertiary method is between $7.50 a barrel and $8.50 a barrel cost to get it out of the ground.

Senator WALLOP. As opposed to the original cost when Bell Creek came on line?

Mr. KEATING. Right.

Senator WALLOP. How much did it cost then?

Mr. KEATING. Lifting cost for an average field is somewhere around $1.80 a barrel for normal lifting costs per barrel. Now, Gary Operating has done an extensive survey for the financing of a tertiary program. And even at $14 or $15 a barrel, they cannot get a fair return on the investment nor can they get banking because of the economics from that study.

The banks say it's too risky and there is not enough return. So, they are stymied right now with their tertiary program.

There is one other study. The Department of Energy joined with Continental Oil on a program out by Teapot Dome. And the number of barrels recovered for the amount of money put in—the cost of extracting that was $50 a barrel when there was a $15 price on it. It's not economical.

Senator BAUCUS. What is the secondary recovery?

Mr. KEATING. Water flooding.

Senator BAUCUS. What does that cost? You said eight, nine something for tertiary.

Mr. KEATING. Tertiary is $7.50 to $8.50. I'm not sure what water flooding costs, because it started in 1968. It's been under a water flood process for 10 years.

Mr. SYLVESTER. I couldn't give you any specifics, because each property is going to vary with the amount of pressure, amount of water it takes and everything else. I think roughly it would double your primary costs as a general rule.

If this $1.80 figure is correct, probably water flooding would run up $3.50, $4.50 additional costs.

Senator WALLOP. So, it would double each time you engaged in a new recovery?

Mr. GEORGE. Not only that, every time you drilled another well, the cost keeps going up, where you spend the same amount of money for drilling a secondary recovery well as you do for the original exploratory well.

Senator BAUCUS. Let me ask a question as to permits. I'm trying to get a sense of which permits are the most burdensome. And all of us like to rail against bureaucracy. Certainly the Congress does, too. We are almost as frustrated trying to deal with bureaucracy as you on the receiving end.

But it would help me and I am sure Senator Wallop too, if you would give me some sense of what permits by which agency are the most burdensome and most ridiculous.

Mr. SHOWALTER. I had some of this prepared and I sent it to Dick Cheney of Wyoming, but I will present it for the record.

I wrote a letter concerning—he was looking into the problems and restrictions that Federal Government is imposing on people when they are trying to look for oil. If we say, "We want you to look for more oil," what problem is that presenting to these people?

Well, the biggest problem in my mind and I think a lot of people's here is, if it's a Federal lease, getting permits to get in there and drill the well. If the property is on a State or private lease, this is what you have to fill out. It costs you about $300 to get a survey. And you type this piece of paper up.

If you are drilling on a Federal piece of ground, even if somebody else is on the surface, this is the paperwork involved. And it costs you $2,000–$5,000 for an uncomplicated location just to do the paperwork. Also in that you have to have maybe, sometimes two or three inspections where you drive to remote locations, say, in South Dakota. You have a BLM person there. You have a USGS person there. You have a drilling contractor there, dirt contractor there, and the rancher, all of them driving six pickups that get 10 miles to a gallon, to get to this location.

They go out there and kick the dirt a little bit. They never change anything significant on what you are going to do out there to drill a well. They certainly never protect any of the environment, because you can't do anything different anyway, unless you are going to drill in the middle of the creekbed, which nobody would, anyway.

The net result is costing you a lot of money.

Also, before you get done, you have to have an archeologist out there, which costs another $600, usually, to inspect the location. If you finally get it approved—and I think Dave True provided numbers relative to what you have to do in addition to what you normally do, based on restrictions imposed by the BLM or Forest Service or USGS that don't really protect the environment and don't really affect what is going on at the location except to increase your costs.

Now, you might not be aware, but if I wanted to drill a 1,000 foot oil well, which we still do occasionally in Wyoming, on a piece of ground, I have to go through all this paperwork. If I want to go in there and drill a uranium test hole, I wouldn't have to notify anybody.

That's the difference between the Oil and Gas Lease Act and the Mining Act.

Senator BAUCUS. Does anybody else have anything to add to that?

Mr. PTASYNSKI. As things keep increasing—we have just recently beat back restrictions proposed by OSHA on benzene. They were practically ready to have everybody that worked in the oil field wear rubberized suits. Finally after a great deal of effort and expense—I'm not sure if it was congressional or executive—came the withdrawal of the possible requirement.

Another one that is coming up is the designation of drilling fluids that are possibly hazardous substances. You notice "possibly hazardous substances." This is what the bureaucrats thought it might be. Since they didn't know for sure, they thought the Government ought to monitor the disposal sites of drilling mines.

We have been drilling wells with mud since 1901. There has never been a case where somebody drowned in a pit. And if a cow does, the rancher is paid for it.

And afterwards, the mud is disposed and the pit is covered over. I don't know that anyone has suffered any damage as a result of this.

Anyhow, since they are not sure it isn't hazardous, they want the industry to monitor these sites for indefinite periods.

By "monitor" they mean fence it off, drill core holes around the site to make sure there isn't any seepage of the possibly hazardous substance, install TV monitors so you can remotely monitor it. I mean, this is ridiculous. It would cost $8 or $9 billion a year to implement this type of regulation.

Senator WALLOP. Let me tell you something that happened on that. This is interesting, because I think we ought to look at it again.

EPA presented a proposal to the Environmental Public Works Committee to get them to give $25 million to look into the hazards of drilling mud.

Somebody asked them the same question: What is the nature of a hazardous mud? They said they hadn't identified it. That's why they needed the $25 million.

Obviously, they were turned down. What they have done is turned to the industry to provide the same funding that they were denied by the Congress.

Senator BAUCUS. What is the status of this that you're talking about?

Mr. PTASYNSKI. I think this thing has been held back, put off for 2 years.

Mr. GEORGE. Was your question as to which agencies are the biggest problems?

Senator BAUCUS. How do you want to answer it? I'm trying to get from your viewpoint what is the biggest problem.

Mr. GEORGE. I think the Forest Service puts more restrictions because of the kind of area you are in. In a lot of cases, the individual people are a lot easier to work with. The Bureau of Land Management seems to be on a blanket basis. It's difficult at any time. If you want that kind of comparison, you can make that.

Senator BAUCUS. You say within the Forest Service it varies?

Mr. GEORGE. With the individuals you are dealing with primarily. Many of them are more reasonable on the average than——

Senator WALLOP. One of the biggest differences between Forest Service and BLM—one of the things that came up from the Department of Natural Resources, the Forest Service still has the ability for most of their land managers to make a number of decisions on their own. And second, the BLM does not have that. They have to get everything approved. And you can never find who ultimately will give you that decision.

When Guy Martin was out of the Society of Range Management, he told me that they have gotten out of hand, that they had really been approving more and more of their land managers' decision. The point is, they don't understand yet what the problem is. If the land managers still have to go back to Washington to get approval for every decision, it's different still from the Forest Service. It doesn't matter how many more they have to approve.

Mr. GEORGE. None of the people that go out with Mr. Showalter at his site can give you an approval on sight. None of them can do that. They must all fill out a form and go back and have their supervisor do it, even though they have no objections for recommending.

In one case I was told I was prevented from moving a fence from private property. I was not allowed to move the fence until the BLM gave us permission to drill. Now they are taking over the authority of the rancher, telling me what I can do with his fence and so forth, even though I had full cooperation of the rancher.

Mr. BURTON. We had to be drilling over July 1, yesterday. And we could have been stopped by the whim of a Forest Ranger. He did stop our rig from moving in. And we were able to placate him by agreeing to put in $30,000 worth of cattle guards, replacing eight existing cattle guards and putting two more in at our expense. They said that these cattle guards that they had were antique and they wanted them replaced.

So, we have to subject ourselves to that kind of blackmail to get these things done. It seems they can make decisions that are way beyond their authority or should be way beyond their authority. But you have to do it because you have to move in. We could have lost 20,000 acres by not drilling over July 1.

Mr. SHOWALTER. I think whether the BLM is worse than the Forest Service or may not be isn't the point. What I think is that Federal control over the right to get a permit to drill an oil and gas well should be removed from the laws. That would be the EPA law and the new BLM organic act.

I think you should go back to requiring one piece of paper like the State does and not a list of requirements where it takes two or three books to interpret and read.

Senator BAUCUS. Even on Federal land?

Mr. SHOWALTER. On Federal land.

Senator BAUCUS. Realistically, I don't think the Federal Government is going to give up control. Couldn't it be done one page?

Mr. SHOWALTER. Yes.

Mr. KELLER. It had been one page and they handled it quickly and it went on.

Mr. SHOWALTER. This is an example of excessive bureaucratics. They figured out a complex method of trying to meet the law so that everybody got a job.

Senator BAUCUS. I would like to include with the transcript the State form.

Mr. SHOWALTER. I have it all.

Senator BAUCUS. Let's put all of those in the record. If any of you want to tell me as quickly as possible the most ridiculous permits or agency procedures, it will be helpful, because obviously we are in a better position to help out.

Senator WALLOP. We are running very close to Senator Baucus' departure time.

I just wanted to ask you because you mentioned it. How optimistic are you that our national production could be dramatically improved under ideal situations?

Mr. PTASYNSKI. I think without decontrol, the IPAA has caculated that by October 1, 1981, we would be producing another 400,000 a day over and above what we would have normally. At the end of 1985, we would be producing between 2 and 3 million barrels a day additionally over what we would be at that time without decontrolling and the excess profits tax.

So, that boils down into quite a bit of oil. But to put it in perspective, I saw Senator Jackson on TV Friday, and he was talking about the great hope of synthetic fuels. His remarks was that we should spend $40 billion—I really listened to that, because it wasn't $40 million. It was $40 billion—between now and 1985 to set up a synthetic fuel industry.

And the interviewer, who was pretty sharp asked him how much of this would be producing at the end of 1985, which caught him by surprise, because he mumbled for awhile. Then he said, "If things work out all right, 19,000 barrels."

What Senator Jackson is proposing is spending $40 billion to get 800 barrels of additional production, whereas the price of domestic crude were decontrolled as the President is proposing in a phasedout matter, in the same time period, in 1985 we will be producing between 2 and 3 million barrels a day additionally. And the Government would receive $40 million in increased taxes under current IRS regulations.

Senator BAUCUS. Why can't you find oil in Washington?

Senator WALLOP. One last question along that line, because the Finance Committee has had two very conflicting pieces of testimony presented to it as to what the cause of the problem is. Some witnesses have told us the present restraint on the oil company expenditures is not money but drilling equipment. And other witnesses have said the exact opposite.

Your experience is drilling equipment? That is the impediment right now?

Mr. PTASHYNSKI. We always come up with the equipment. Here a few years ago when we hit a bind, the Canadians were treating their operators the way our Government is currently treating ours. They had price rollbacks, cuts and depletion allowances. They said, "To hell with it." And they came down here and drove the Canadian drillings rigs. We put them to work.

Now they are on their way back up to Canada because for instance, they have increased their depletion allowance there to 30 percent where ours has been cut to 20 and is on its way out. So, they were finding oil up there in great amounts.

Mr. BURTON. Senator, I would like to point out one thing. Maybe Senator Gravel from Alaska could show you some of the seismic features offshore in the Bering Strait and in the Bering Sea. They have tremendous anticlines out there that potentially have billions of barrels of oil that are unleaseable at this time because they are in a moratorium or something, something more or less like the east coast was. And these things are available. These seismic sections are available through seismic contractors. And the USGS and BLM have these things purchased. They furnished these seismic contractors who shoot only on the speculation they might be able to sell it.

They have a built-in customer in the U.S. Government, so they can afford to shoot it and sell it to the major companies mainly, but they are available for your inspection.

You can go to their office in Anchorage and look at the seismic contractors' records that he keeps. And you can see tremendous structures.

Like I say, if you have a geologist on your staff, he could give you a basic estimate of the potential of reserves in offshores Alaska that are untappable right now because they can't be released.

Senator WALLOP. Gentlemen, I hate to call this to an end. Senator Baucus must go.

Max, I really do appreciate it.

One thing I want to ask, because some people who were going to testify on either the environmental or the consumer side, and they were simply not able to be here.

Is there anyone in the audience now that would like to make a comment on those proposals, on the proposed windfall profits tax as it relates to either the consumer's interest or the environmental interest?

[No response.]

Senator WALLOP. They were invited here but they were simply unable to make it.

I just wanted the record to show that Senator Baucus and I wanted to have a fair representation today. They had been invited.

Mr. SHOWALTER. Could I make one comment. You had a question in regards to are the rigs available. I don't remember the exact numbers, but from 1973, the number of wells have increased 50 percent. Somewhere we had to come up with another 50 percent of the rigs available to do that.

The drilling industry, which is paid by the operator, was able to do that.

Along the same vein, they have used these reserve estimates and said, "If there is only x number of barrels to be found, that's not going to solve the problem, so we are not going to provide any incentive." It's the same kind of logic. I think the rigs will be there if they want to drill and the contractor can make money.

Mr. PTASYNSKI. If the next remark is: "Can you manage them," well, we manage them if we can get them.

Senator WALLOP. Probably the fact you increased more than 50 percent is because the number of delays of down time that you have.

Mr. GEORGE. You're still not convinced that the price of oil doesn't stimulate activity. The chart that Don Basko submitted is probably one of the most significant pieces of evidence you have today of only 250 well permits in one month just on a speculation that you are talking about $20 oil. That's the major word, "speculation."

Senator WALLOP. Thank you very much, to all who testified. We appreciate it.

[Thereupon, at 2 p.m. the subcommittee recessed, to reconvene at the call of the Chair.]

[By direction of the chairman the following communications were made a part of the hearing record:]

TESTIMONY BY STEPHEN TARVER, GILLETTE, WYO.

My name is Stephen Tarver. I'm an accountant and I live at Gillette. Wyoming. I want to express my appreciation for this opportunity to express my views on energy tax legislation before an official Congressional Committee.

First of all I must frankly admit that I do not clearly understand exactly what is being proposed in the way of an excess profits tax on oil. As I understand it there are several different proposals including a tax without any plowback exemptions and tax with plow-back exemptions. There seems to be no concensus of opinion of what would be the result in either case.

I would like to propose some alternative tax legislation which I believe would go much further toward solving the energy problem and the many problems resulting from it, than any kind of excess-profits tax on oil.

This proposed legislation could not only result in no more increase in the price of oil but it could result in the United States achieving energy self-sufficiency within a very few years. It could very possibly result in causing the OPEC nations to become very willing to sell us all of the oil we want to buy as soon as we want to buy it at a very reasonable price.

Under existing tax legislation, much of which has been in effect for over 50 years, the extractors of minerals and fossil fuels such as oil and coal have been given a production allowance making it possible for them to escape the income tax entirely on up to 50 percent of their net income from such extraction.

This tax allowance has come to be known as the percentage depletion allowance. It is not, and I repeat, it is not a depletion allowance at all because it is not based on the amount of the deposit depleted. It is a percentage production allowance because it is based on a percentage of the production wth no regard whatever for the percent of the deposit depleted.

As further evidence that this is not a depletion allowance, in most cases over 80 percent of the allowance goes to the taxpayer who only leases the mineral deposits and extracts the minerals while less than 20 percent usually goes to the taxpayer who actually owns the mineral deposits which are actually being depleted.

This production allowance worked very well until the OPEC oil cartel was formed. As long as there was free competition there was ample production to keep the price of oil very low. This abundance of oil was undoubtedly a deciding factor in the winning of World War II.

My proposal would be to write a provision into the tax law to give a comparable production incentive to those taxpayers engaged in the production of alcohol for automobile fuel, methane gas to be used as natural gas is now used, windpowered generators to generate electricity and solar collectors to provide space heating and water heating as well as equipment to produce alcohol and equipment to produce methane gas.

In view of the success which this production allowance produced in stimulating the production of oil and gas for nearly 50 years, there is every reason to believe that a similar production allowance could result in the large scale production of energy in usable forms from inexhaustible sources of abundant energy such as the sun, the wind, wastes and re-growable plants.

Of course there are those who feel that any tax incentives to encourage the use of the alternative energy sources should go to the consumer. In fact some such income tax credits are already allowed by law to purchasers of solar collectors and wind-generating equipment. However, most people do not seem to understand that by giving these tax incentives to the consumer without giving any incentives to the producers simply creates an increased demand for a limited supply, thereby driving the price of such equipment up by far more than amount of the tax credit given to the consumer for buying it.

One need only to consider the enormous increase in the price of farm machinery, as an example, in the last 17 years since the investment tax credit went into effect, to realize that the investment tax credit is undoubtedly one of the greatest causes of inflation in this country today.

Of course there are also those who will argue that it will be three or four decades before these inexhaustible energy sources can provide even a significant portion of our energy. Unless we change our tax laws what they say is probably correct because the available risk capital will undoubtedly be attracted to where the tax advantages are which is, of course, to the exploiting of our dwindling supply of fossil fuels.

It would not be because we do not have the technology in these alternative energy fields. We have that technology.

Over 35 years ago the S. Morgan Smith Company of York, Pennsylvania built a large windpowered generator at Rutland, Vermont. It generated 1,250 kilowatts of electricity and was integrated into the power grid of the Central Vermont Public Service System. It proved that generating electricity with windpower on a large scale was commercially feasible. The only reason that the commercial generation of electricity with windpower was not further developed was because of the cheap oil resulting from the so-called percentage depletion allowance.

Solar energy has been used for heating for decades in Israel and Australia ~~but~~ it was never developed on a large scale in the United States because of the abundance of cheap natural gas resulting again from the so-called percentage depletion allowance.

More and more cities are turning their municipal wastes into fuel and re-cycleable metals. The technology for doing this has been around for a long time-so why haven't we been using it before instead of polluting our land and water? It's the same old story. The tax laws allowed enormous tax advantages for digging this fuel and metal out of the ground but it allowed no tax advantages for producing fuel and re-cycleable metals from wastes. So why bother re-cycling wastes to get fuel and metal while one had to pay up to 91 percent in income tax on any profits, when you could dig them out of the ground and escape the income tax entirely on up to 50 percent of your net income?

There is no question about whether we have the technology to generate electricity with windpower. That is a well proven fact. There is no question about whether we have the technology to produce usable heat from the sun. That is a well-proven fact. Neither is there any question of whether we have the technology to produce alcohol for automobile fuel and methane gas for heating, from wastes and re-growable plants, that is a well proven fact. Then what is the question?

Many people in government would like us to believe that there is a question of whether energy from these inexhaustable sources is or will be cost-competitive with fossil fuels and uranium. But that is not really the important question either. The important question is this. "would energy from these inexhaustible sources be cost competitive with fossil fuels and uranium if a tax incentive were given to stimulate the development of these inexhaustible energy sources comparable to the tax incentives which has been given for over 50 years to stimulate the extraction of minerals and fossil fuels?" That question will never be answered until we try giving such a tax incentive to stimulate the development of these inexhaustible energy sources.

Another important question is this. "What would it cost the government to try giving the producers of windpower electric generators, solar collectors, alcohol for automobile fuel, methane gas for heating, equipment to distill alcohol and equip~~ment to~~ produce methane gas, a percentage production allowance comparable to that given to the producers of oil, gas, coal and uranium? The answer is that it wouldn't cost us anything if it didn't work. If there were no production there would be no tax deduction. It wouldn't be like to government giving out billions of dollars in research grants which don't produce any worthwhile results. That money is lost for certain.

On the other hand, if it did result in large scale production, the revenue loss would probably not be any greater than the present loss from the percentage depletion allowance on fossil fuels which would be replaced.

Furthermore if such an industry did materialize, it would provide many thousands of jobs which would mean that many more wage-earners would be paying income tax into the government and there would also be fewer people drawing unemployment compensation from the government.

In addition, such an industry could probably produce such equipment for sales to other countries. Thus instead of having money going out of this country for the purchase of oil, we would likely have money coming into this country from the sale of equipment. So there are several ways we could possibly gain from such tax legislation but no way that we could lose from such tax legislation.

For years Congress has been voting in income tax deductions and income tax credits to encourage the public to invest in all sorts of things. In addition to the percentage depletion allowance, there is the investment tax credit, the residential energy credit, the capital gains deduction, the individual retirement account deduction, the work incentive credit and the new jobs credit. Congress has even written a tax credit into the law to encourage people to contribute to its members' campaign funds called the Credit for Contributions to Candidates for Political Office.

Why then shouldn't Congress allow a tax deduction or credit to encourage the production of clean energy from our inexhaustible sources of abundant energy to help solve one of the most serious problems this country has ever faced?

As I understand it there is very serious consideration being given to allowing a $3 per barrel production tax credit on oil produced from oil-shale which would figure out to 15 percent on $20-a-barrel oil. Why not give a 15 percent production tax credit to the producers of alcohol for automobile fuel, and to the producers of methane for heating and to the producers of windpowered generators to generate electricity and to producers of solar collectors to produce heat and to makers of equipment to produce methane gas and to producers of equipment to distill alcohol?

A study on the feasibility of windpower was made and published in 1975 by the Mitre Corporation of McLean, Virginia under a grant from the National Science Foundation. I would like to read two short excerpts from that study.

ECONOMICS

An important measure of the economic viability of WECS is the cost of electricity produced by such systems. This cost is, currently, still relatively large compared to that of fossil-fueled systems. However, the unit price of wind turbines is expected to decrease as the size of the units is increased and as mass-production techniques are introduced. Present estimates indicate that WECS, if located at sites with reasonably high average wind velocities, would be expected to produce electricity at busbar prices of 20 to 30 mills per kilowatt-hour. This would be competitive with conventional diesel electrical generation plants using oil priced from $10 to $11 per barrel or higher.

Wind systems without energy storage may be tied into a conventional system, powered, for instance, by a diesel generating plant and used to save fuel when the wind is blowing. On the other hand, wind systems with suitable energy storage capabilities can be used as a complete substitute for a conventional electric generating plant. In other case, the break-even points might be expected to occur at fuel prices of about $10 to $11 per barrel of oil for sites with average wind velocities of about 15 mph. To achieve these break-even prices at more moderate wind velocities will require development of systems with improved performance or lower costs.

WIND DISTRIBUTION

Currently available maps showing patterns of average wind power over the United States provide only very rough estimates of this power. Many are based mainly on measurements obtained near ground level at airports. However, airport locations are, generally, purposely chosen to avoid sites where local topography might result in high wind speeds. Other pattern maps are produced by extrapolating high altitude wind measurements down to a standard height above ground level. An example of the latter type is shown below. Its shaded areas indicate where average wind speeds are estimated to equal or exceed 18 mph at 150 feet altitude over the United States. Many of these areas are near large population centers such as New York, New England, Western Texas, Denver, Colorado Springs, Los Angeles and San Francisco. Others are areas served by large utility networks such as those of the Bonneville Power Administration and the Tennessee Valley Authority.

A rough integration of the average power available within the 18 mph contour surrounding the high Great Plains region indicates that with conservative assumptions regarding the operating efficiencies and proper spacing of wind machines, it is expected that the power that could be extracted from the winds in that region, alone, is several times the present United States electrical power demand.

We are constantly being reminded to conserve energy. Yet there is far more energy going to waste every day in this country in the form of unharnessed windpower being dissipated across this country than we are consuming in all of our homes, farms, factories and automobiles combined and yet Congress has offered no meaningful tax incentive whatever to encourage the production of wind-powered generators to convert this abundant inexhaustible supply of clean energy into a usable form.

Henry Ford was quoted in the December 7, 1929 issue of the Literary Digest on Page 29 as saying, "We can get fuel from fruit, from that sumach by the roadside, or from apples, weeds, sawdust—almost anything. There is enough alcohol in one year's yield of an acre of potatoes to drive the machinery necessary to cultivate the field for a hundred years."

Still in 1979 the Federal Government is paying farmers to leave some 22 million acres of cropland to lie idle and to *not* produce crops from which alcohol for automobile fuel could be produced.

A process has recently been developed at Purdue University by which organic waste can be economically converted into alcohol. The Indiana legislature was so impressed with it that took the very unusual step of appropriating two million dollars to specifically further this development.

There are approximately one billion tons of organic waste produced in this country annually. Dr. Tsao, the man primarily responsible for developing the process at Purdue, estimates that with his process this one billion tons of organic waste could be converted into approximately 100 billion gallons of fuel-grade alcohol. The United States now consumes approximately 100 billion gallons of gasoline annually.

What we have in the United States is not an energy shortage. What we have in this country is a shortage of the means of converting our abundant supply of energy from inexhaustible sources into useable forms of energy.

It seems to me that the quickest and surest way to achieve energy independence in this country would be to produce the means to turn that abundance of energy from inexhaustible sources, into usable forms of energy.

When World War II started the manufacture of automobiles for civilian use in this country was brought to a complete halt. I recently heard a statement to the effect that there will be some 15 million automobiles manufactured in this country this year.

If the threat to the security of this country because of our dependence on foreign oil and our enormous foreign trade deficit, is as serious as many people think it is, it seems that it's about time we started encouraging our automobile manufacturers as well as other manufacturers to start shifting some of their manufacturing facilities to the manufacture of windpowered electric generators, solar collector, methane gas generators and alcohol distillaries.

When Hitler started World War II, the free nations of the World had few arms. It didn't take 10 years or 15 years or 20 years to arm those nations. In five years the United States armed the greatest war machine this world has ever known. Three months after Pearl Harbor, in early 1942, 90 percent of the world's natural rubber came under the control of the enemy. By the end of the War in 1945 the United States was synthetically producing 87 percent of the rubber it was using.

I am thoroughly convinced that with its industrial might, the U.S. could very well produce the means to convert our abundance of energy from inexhaustible sources into usable forms of energy in a very few years if we had a tax system which encouraged American industry to do so instead of a tax system which discourages it from doing so.

I do not beliece the Arabs are so dumb but what they could likewise be convinced of the same thing.

I believe that one of the most important things that should be remembered is, that by adopting such proposed tax legislation we have everything to gain and nothing to lose. At the same time, by *not* adopting such tax legislation we have nothing to gain and everything to lose.

JOHN J. CHRISTMANN AND CHRISTMANN ASSOCIATES,
Lubbock, Tex., July 5, 1979.

Senator MIKE GRAVEL,
Senator MALCOLM WALLOP,
Senator MAX BAUCUS,
Energy Subcommittee,
Senate Finance Committee.

Re Windfall Profits Tax.

GENTLEMEN: Due to the limited time you had in Casper on July 2nd to hear testimony, it was recommended that I submit a written statement. It is my feeling that many of the following points may not be brought out so please bear with me and consider these.

First, the term "Windfall Profits" is an outright misrepresentation since the tax is in no way related to the profit an operator makes on a given operation. Citibank of New York has determined that over the decade 1968–1977 the petroleum industry averaged a 13.9 percent return as compared to 13.3 percent for all U.S. manufacturing. During the last year of that decade, the petroleum industry fell below manufacturing at large with a 14.2 percent return compared to 15 percent across the board. The recent decline in relative profitability is due in part to U.S. controls on crude oil pricing which has held price increases essentially to the nations implicit price deflator index. The above average return figures include the "Obscene Profits" of the Internationals. Domestic Independents return would be considerably less than manufacturing at large.

Unfortunately for the producer, his costs in oil exploration and production have far exceeded that index, creating for him a cost-price squeeze which greatly diminished his available capital for further exploration. Since 1972, for example, while the implicit price deflator was climbing 52% thru 1978, oil field machinery costs rose 105%, oil well casing rose 112%, oil field wages climbed 80% and drilling costs moved upward by 113%. The tax could well leave many potential secondary recovery projects in an operating loss position resulting in their premature abandonment.

The "Major Oil Company's Obscene Profits" as they have been called by the critics result entirely from their overseas operations and the fact that the Major Companies have all phases of the industry from which to reap a profit. Neither of these two highly profitable sources are available to the domestic independent operator who derives his entire income from the sale of oil and gas at the wellhead. This same independent is the one who drills 80% of the wildcat wells and finds 80% of the reserves in this country. This so-called "Windfall Profits Tax" will take from the real oil finder his only source of funds with which to expand our domestic production.

Small wonder that the Major Companies spend the greater part of their exploration efforts overseas. I, quite frankly, am presently considering a concession in Nigeria where we can invest 150% of domestic costs and sell our product for almost 400% of our old oil price here sold subject to the so-called "Windfall Profits Tax". Why spend our money at home?

The congress seems to think they are better qualified to solve our energy problem with the billions they will take from the professional and highly trained oil operators than to let them invest these funds in additional oil and gas production and alternate fuels with their extensive expertise in these fields.

According to Hughes Tool Co. the rig count in the Rocky Mountain Region this week is 2,017 compared to 2,282 one year ago, down 275 rigs. And this should be the most active time of year. Unless the Domestic Independent Producer is exempt from the so-called "Windfall Profits Tax" or at least allowed to plow the entire tax back into domestic drilling and production the active rig count will drop dramatically from present activity.

Increased domestic oil and gas production is the quickest and surest relief for our immediate problem. It is available if the people who know how to find and produce it are left with sufficient funds to do the job in a favorable economic climate.

Please remember, those "Obscene Profits" were only made by the major International Companies, and to tax the small domestic producer because of them is like throwing the baby out with the bath water.

The house members undoubtedly needed to have something to show the irate consumers that they had found a scapegoat to blame for the higher prices and gas lines, so passed the "Windfall Profits ----" before leaving for home. We have always relied on the Senate for sound judgement in the past and it appears the same holds true in the present instance. However it is high time that the representatives think more of the national welfare than of their re-election. We have our fingers crossed.

Very truly yours,

JOHN J. CHRISTMANN.