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Introduction
Good morning, my name is Katherine Morrison and I'm Staff Attorney working on energy and global warming issues for the U. S. Public Interest Research Group, or U.S. PIRG. U.S. PIRG is the national office for the State PIRGs, which are environmental, good government and consumer advocacy groups active around the country. Thank you for the opportunity to speak today.

The state PIRGs have a long history of working for a clean affordable energy future. Our goal is shift from polluting and dangerous sources of energy such as nuclear and fossil energy to increased energy efficiency and clean renewable energy sources.

Today I will be addressing the issue of our dependence on oil and gasoline prices, especially focusing on policies that should and shouldn't be included in energy legislation. Overall we are dismayed that the energy bill, H.R. 6, passed by the House takes us in the wrong direction.

Summary
Retail gasoline prices have hit over $2.00 a gallon across the country, and the U.S. remains dangerously dependent on oil. The United States holds only 3 percent of the world's oil reserves and uses 25 percent of the world's produced oil. As a result, consumers pay prices at the pump that reflect the stability of overseas oil supplies as well as the often-dubious market behavior of domestic oil corporations.

Congress and the Bush administration proposals will not solve these problems. In May 2001, the Bush administration released its national energy policy, the product of Vice President Cheney's energy task force, which outlined a plan that continues to rely heavily on oil, other fossil fuels, and nuclear power to meet the country's energy needs. In April 2005, the House passed an energy bill does nothing to make cars go farther on a gallon of gas. The bill also does nothing to protect consumers from price manipulations by large oil and gas corporations and, in fact, provides these corporations with new tax breaks and subsidies. The Energy Information Administration (EIA) concluded that the policies outlined in outlined in last year's virtually identical bill would increase U.S. imports of foreign oil by 85 percent by 2025 and do nothing to lower gasoline prices in the short or long-term. In fact, the president recently acknowledged that the bill "wouldn't change the price at the pump today."

Similarly, the Bush administration's proposal to drill in the Arctic National Wildlife Refuge would do nothing to solve our energy problems. EIA has reported that drilling in the Arctic Refuge would not have any impact on world oil prices; the U. S. Geological Survey estimates that the oil found in the Arctic Refuge would meet the energy needs of the U.S. for less than one year. Increasing the fuel economy of our cars to 40 mpg, however, would save at least four times as much oil each day by 2020 as the Arctic Refuge would produce each day at its peak.

The best way to reduce our dependence on oil and save consumers money at the pump is to make cars go farther on a gallon of gas. Today, fuel economy is at a 24-year low of 20.8 miles per gallon (mpg). The National Academy of Sciences has stated that we already have the technology to make cars get 40 mpg. In May 2001, when announcing his national energy strategy, President Bush had the opportunity to take a bold step forward and increase the fuel economy of cars and SUVs to 40 mpg by 2012. If he had, consumers and the U.S. economy already would be reaping the benefits as more efficient cars entered the market. In 2005 alone:

- The U.S. would be consuming 350,000 barrels of oil less per day. This is more than half of our current imports from Iraq.
- Consumers would be saving more than $5 billion at the gas pump, about $300 per new vehicle on the road.
- The U.S. would be offsetting 23.9 million tons of carbon dioxide, the primary global warming gas. This is the equivalent of removing four million average vehicles from the road.

After 2005, as more cars meeting the new standards replaced older, less efficient cars, the benefits would have grown even larger. The big oil companies and automakers continue to fight this progress; in fact, while consumers are paying more

at the pump, oil companies are recording huge profits. Over the last decade, with little resistance by federal regulators, oil companies have merged into mega corporations with the ability to manipulate supply. These mega corporations, the first to benefit from high gas prices, are reaping huge profits while consumers pay more at the pump. In 2004, the top ten oil companies enjoyed net profits of $100 billion, an increase of more than 30 percent from 2003.

Congress has wasted four years on an energy policy that won't help consumers or reduce our dependence on oil. Congress should reject the reject the energy bill. Instead, the Bush administration should ask the Secretary of Transportation to use his authority to increase Corporate Average Fuel Economy standards to 40 miles per gallon. His authority enables any increase that represents the "maximum feasible" standard consistent with technological feasibility, economic practicability, the effect of other government regulations on fuel economy, and the nation's need to conserve energy. A 40 mpg fleet wide standard is consistent with the criteria. In addition, policy-makers should strengthen federal anti-trust laws to give the Federal Trade Commission (FTC) greater market enforcement capabilities and to specifically prohibit companies from intentionally withholding supplies to drive up prices. The FTC should block mergers that make it easier for oil companies to manipulate gasoline supplies and take steps, such as forcing companies to sell assets, to remedy the situation. Finally, the Bush administration should conduct a study of the reasons for the closure of more than 50 refineries in the past ten years and assess how to expand refinery capacity.

The Problem

The United States is simply too dependent on oil. The United States holds only two percent of the world's oil reserves. It produces 10.4 percent of the world's petroleum but consumes 25.5 percent of the world's total petroleum production. Our heavy reliance on oil products to fuel transportation vehicles takes a heavy toll on the environment. Oil pollutes the environment from the point of extraction to combustion, leaving a trail of oil spills, smog-forming air pollution, and global warming in its wake.

Consumers pay a price too in the form of unpredictably high gasoline prices at the pump. Gasoline prices are sensitive to crude oil supply disruptions; moreover, as oil demand increases, so does the price of a gallon of gasoline. Gasoline averaged more than $2.00 per gallon during the first four months of 2005. Rising gas prices are cutting into consumer and business confidence, as well as spending power, which helped slow the U.S. economy in the first quarter of 2005.

The Solution

The best way to reduce our dependence on oil and save consumers money at the pump is to make cars go farther on a gallon of gas. In response to the Arab oil embargo of the early 1970s, Congress implemented the first miles per gallon (mpg) standards in 1975 to protect consumers from high gasoline prices and supply vulnerability resulting from U.S. dependence on foreign oil. The drafters of the successful oil savings law recognized that the only way to reduce dependence on foreign oil was to reduce oil demand, requiring cars and light trucks to nearly double miles per gallon averages to 27.5 and 20.7 miles, respectively. As a result, consumers were able to go farther on a gallon of gas; these standards also had the benefit of reducing tailpipe emissions, including emissions of global warming gases. Cars today use 2.8 million barrels of oil per day less than they would have under the old fuel economy standards.

The 1975 oil savings law also requires that the National Highway Traffic Safety Administration (NHTSA) continuously review and increase miles per gallon standards as technologically feasible.

A 1996 Department of Transportation appropriations bill rider prevented NHTSA from even studying the need and the technological feasibility of new fuel economy standards. In 2001, the Senate retracted this rider and agreed to study fuel economy standards. Congress ordered the National Academy of Sciences (NAS) to determine the effectiveness of the Corporate Average Fuel Economy (CAFE) program and make recommendations for moving forward with new standards.

In 2001, NAS identified ranges of fuel economy improvements for both cars and trucks while holding acceleration, performance, size, accessories, amenities, mix of vehicle types, makes, and models sold constant. The result was a 2002 NAS report, Effectiveness and Impact of Corporate Average Fuel Economy (CAFE) Standards, which concluded that automakers could use existing technology to increase the fuel economy of their fleets to 40 mpg over the next decade while improving safety and maintaining performance.

The technology is available today to make cars and light trucks go farther on a gallon of gas. The Toyota Prius, which gets an estimated 60 mpg in the city, and the Ford SUV Escape, which gets about 35 mpg in the city, demonstrate that foreign and domestic manufacturers can produce smarter engines, more efficient transmissions, and other design improvements to make substantial gains in fuel economy.

Despite the advances in technology, average fuel economy is at a 24-year low of 20.8 mpg for model year 2004 cars and light trucks – six percent lower than the peak value of 22.1 mpg achieved in 1987 and 1988 (Figure A).

The overall declining trend in new light-vehicle fuel economy is due to the recent light truck and SUV boom. "Light trucks" (minivans, pickups, and SUVs) are defined as weighing less than 8,500 pounds. Because fuel economy standards separate light trucks as a class and subject them to different fuel economy standards, automakers often add weight to their trucks to exempt them from the miles per gallon standards altogether. The number of SUVs registered in the U.S. during 2002 increased 56 percent from 1997.

High gas prices, however, have slowed SUV sales. General Motors' sales fell almost eight percent in April 2005 from the same month a year earlier, primarily because of weak demand for SUVs. This drop in demand also hurt Ford, which sold five percent fewer vehicles in April compared with a year ago. At the same time, demand for hybrids and other more fuel-efficient foreign sedans is surging.

Figure A. Fuel Economy Average, by Model Year, 1975-2004

U.S. EPA, "Light-Duty Automotive Technology and Fuel Economy Trends: 1975 Through 2004, at http://www.epa.gov/otaq/fetrends.htm.

The Current Proposals

In May 2001, the Bush administration released its national energy policy, the product of Vice President Cheney's energy task force, which outlined a plan heavily focused on oil, other fossil fuels, and nuclear power to meet our energy needs. Moreover, the Bush-Cheney energy policy offered no plan for increasing the fuel economy of America's cars and trucks to reduce oil demand. For four years, the Bush administration has tried to push its energy plan through Congress while actively opposing proposals to significantly increase the fuel economy of cars and light trucks.

In April 2005, the House once again passed an energy bill, H.R. 6, which does not include any provisions to increase fuel economy or otherwise reduce oil demand. Instead, the 2005 House energy bill provides the oil and gas industry with $3.2 billion in new tax breaks, or more than 40 percent of the total package. Meanwhile, the House dropped more than $3 billion in incentives for renewable energy and energy efficiency in this version of the bill. According to a recent analysis by the Energy Information Administration (EIA), by 2025, U.S. imports of petroleum would increase by 85 percent under the Bush administration's preferred energy policy, encapsulated in the 2003 federal energy bill, which is nearly identical to the version passed by the House in April. EIA also found that the energy bill would actually slightly increase gas prices by 2010 compared with business as usual. The president himself admitted that the bill "wouldn't change the price at the pump today." Regardless, the president continues to push Congress to pass this energy bill.

Similarly, the Bush administration's proposal to drill in the Arctic National Wildlife Refuge would do nothing to lower gas prices or reduce our dependence on foreign oil. The U.S. Geological Survey assessment of the coastal plain estimates that the oil found in the Arctic Refuge would meet the energy needs of the United States for less than a year. Even if we started drilling today, that oil would not reach American consumers for at least 10 years. EIA recently reported that drilling in the Arctic National Wildlife Refuge would not have any impact on world oil prices, noting that "[a]ssuming that world oil markets continue to work as they do today, the Organization of Petroleum Exporting Countries could countermand any potential price impact of ANWR coastal plain production by reducing its exports by an equal amount." Opening up the coastal plain of the Arctic Refuge would not solve our energy problems. Increasing the fuel economy of our cars to 40 mpg, however, would save at least four times as much oil each day by 2020 as the Arctic Refuge would produce each day at its peak.

Our Recent Findings

The Bush administration has failed to apply our technological know-how to improve the fuel economy of America's cars and SUVs, which has lead to higher prices at the pump, increased dependence on foreign oil, and a host of environmental problems stemming from oil exploration and combustion.

On Tuesday, on the anniversary of the release of the Bush-Cheney plan, we are released a new report, America Idles: President Bush's Inaction Costs Americans $5 Billion at the Pump in 2005. We examined what would be happening if four years ago, the President had picked up a pen and taken a bold step forward by increasing the fuel economy of cars and SUVs to 40 miles per gallon by 2012. Even though we would still be phasing in the fuel economy standards, more efficient cars would already be entering the market. By 2005, new fleets of cars and light trucks would have averaged almost 30 mpg, or nearly 10 mpg more than they average today.

If President Bush had raised fuel economy standards in May 2001 to 40 mpg by 2012, in 2005 alone we would see the following benefits:

- The U.S. would be consuming 350,000 barrels of oil less per day. This is more than half of our current imports from Iraq.

• Consumers would be saving more than $5 billion at the gas pump, or about $300 per new vehicle.

• The U.S. would be offsetting 23.9 million tons of carbon dioxide, the primary gas responsible for global warming. This is the equivalent of removing four million average vehicles from the roads.

After 2005, as more cars meeting the new standards replaced older, less efficient cars, the benefits would have grown even larger.

The Oil Companies

Politicians at the federal level and oil industry representatives are putting the blame for rising gas prices on everything from the Organization of Petroleum Exporting Countries (OPEC) to fuel additive requirements. While OPEC plays a role in determining gas prices, this finger pointing overlooks the fundamental problem: America is too dependent on oil. As long as demand for oil continues to climb, consumers will remain vulnerable to price spikes at the gas pump—whatever their cause.

It is instructive, however, to examine some of the other market factors that drive gasoline price spikes, in addition to growing demand. Over the last decade, with little resistance by federal regulators, oil companies have merged into mega corporations with the ability to manipulate supply. These mega corporations, the first to benefit from high gas prices, are reaping huge profits while consumers pay more at the pump.

Although consumers continue to suffer at the pump, oil companies are enjoying huge profits. In 2004, the top ten oil companies enjoyed net profits of $100 billion, an increase of more than 30 percent from 2003. According to its 2004 annual report, ExxonMobil earned a record-breaking $25.3 billion in net income in 2004, a $3.8 billion increase over 2003 and a $13.9 billion increase over 2002. Cash flow from operations and asset sales was $43.3 billion, also a record. In addition, the company handed out nearly $15 billion to shareholders in dividends and share buybacks. During the year ending December 31, 2003, CEO Lee Raymond earned $27.8 million in salary and bonuses and exercised $15.9 million in options. In 2004, Raymond received a 37 percent pay increase to $38 million—about half a day's profits at the company.

The world's four largest oil companies, Shell, BP, ExxonMobil and ChevronTexaco, have earned a combined $23.8 billion during the first three months of 2005 alone.

Federal regulators have allowed multiple large, vertically integrated oil companies to merge into even larger entities, enabling them to exploit supply and demand to increase profits. Because people use gasoline to get to work, the grocery store, and school, the demand for gasoline is inelastic, meaning that demand does not change despite increases in price. Americans' reliance on oil products in their daily lives places them in the hands of the small number of multinational corporations that now control the bulk of the refineries and market for oil and gas in the United States.

In 1981, 189 companies operating in the United States owned 324 refineries; by 2001, 65 firms owned 155 refineries. The market share of the top ten largest refiners grew from 55 percent to 62 percent over the same period of time. Today, the top ten refineries control 78.5 percent of domestic refinery capacity while the five largest oil companies (ExxonMobil, ChevronTexaco, ConocoPhillips, BP and Royal Dutch Shell) control half of all domestic refinery capacity. In addition, together they own 48 percent of domestic oil production and 61.8 percent of the retail gasoline market.

The mergers in the oil industry have forced the closing of many refineries, creating highly concentrated or "tight" markets in many states. The Federal Trade Commission (FTC) and the Department of Justice (DOJ) guidelines state that "mergers should not be able to enhance market power or facilitate its exercise. Market power to a seller is the ability to profitably maintain prices above competitive levels for a significant period of time." Sellers may also lessen competition on dimensions other than price, such as product. "The result of the exercise of market power is a transfer of wealth from buyers to sellers or a misallocation of resources."

The government gains its authority to review mergers and acquisitions under Section 7 of the Clayton Act. Section 7 prohibits mergers and acquisitions that may substantially lessen competition or tend to create a monopoly (ownership of one). The FTC and DOJ measure market concentration with the Herfindahl-Hirschman Index (HHI).

Under the HHI, market concentration is equal to the sum of the squares of the individual market shares of every firm in the market. For example, if there were only four firms in a particular market, each with 25% of the market, the HHI would be 2,500 (252 x 4). Any market with an HHI over 1,800 is considered highly concentrated by the enforcement agencies and viewed with some suspicion; between 1,800 and 1,000 the market is considered moderately concentrated; and below 1,000, the enforcement agencies consider such markets to be unconcentrated.

Where products are relatively undifferentiated, the FTC and DOJ guidelines also find that a merged firm may lessen

competition through unilaterally raising prices and suppressing output where the merged firm owns a combined market share of at least 35 percent. The merger provides the merged firm a larger base of sales on which to enjoy the resulting price rise and also eliminates a competitor to which customers otherwise would have diverted their sales.

If a merger does not pose a serious threat to competition, it is unlikely to be challenged. If a substantial threat is present, however, the enforcement agencies may exercise discretion to prosecute.

A recent investigation by the FTC into 2000 Midwest price spikes disclosed unilateral actions by firms to manipulate the market to increase prices. An executive of one of the companies made clear that he "would rather sell less gasoline and earn a higher margin on each gallon sold than sell more gasoline and earn a lower margin." This evidences the business practice of lessening competition through the suppression of a product to increase price. But despite the oil executive's blatant admission that he was responsible for withholding supply to drive up price, the FTC found that "a decision to limit supply does not violate antitrust laws…Firms that withheld or delayed shipping additional supply in the face of a price spike did not violate antitrust laws."

In 2000, 28 states were considered moderately concentrated, and nine states had an index above 1800 and were thus considered "highly concentrated." As a point of comparison, in 1994, as measured by the HHI, the gasoline wholesale market was "moderately concentrated" in 22 states (see Appendix B).

A few mega firms are gaining an exceedingly larger market share, enabling them to control the flow of gasoline in the U.S. This provides the opportunity to manipulate the market to turn a quick profit, because no standards govern selective pricing or withholding of supply. These firms individually own such a large percentage of the industry as a whole that collusion is not needed to manipulate the market. If they so chose, individual actions would be sufficient to upset the supply in any given sector. As long as there is no collusion involved, firms are free to set prices and withhold supply to increase gasoline prices and turn higher profits.

Conclusion

Congress has wasted four years on an energy policy that won't help consumers or reduce our dependence on oil. Congress should reject the reject the energy bill. Instead, the Bush administration should ask the Secretary of Transportation to use his authority to increase Corporate Average Fuel Economy standards to 40 miles per gallon. His authority enables any increase that represents the "maximum feasible" standard consistent with technological feasibility, economic practicability, the effect of other government regulations on fuel economy, and the nation's need to conserve energy. A 40 mpg fleet wide standard is consistent with the criteria. In addition, policy-makers should strengthen federal anti-trust laws to give the FTC greater market enforcement capabilities and to specifically prohibit companies from intentionally withholding supplies to drive up prices. The FTC should block mergers that make it easier for oil companies to manipulate gasoline supplies and take steps, such as forcing companies to sell assets, to remedy the situation. Finally, the Bush administration should conduct a study of the reasons for the closure of more than 50 refineries in the past ten years and assess how to expand refinery capacity.

BIOGRAPHY – Katherine Morrison

Katherine Morrison is a staff attorney working on energy and global warming issues with the U.S. Public Interest Research Group (U.S. PIRG). She is responsible for policy development, research and advocacy on energy issues ranging from electric utility restructuring to gasoline prices and renewable energy. She is on the on the Steering Committee of the U.S. Climate Action Network.

Before joining the U.S. PIRG staff in 2001, she worked with the Natural Resources Defense Council as the Communications Coordinator for the Clean Air Network and with the Center for International Environmental Law. She is 1994 graduate of American University, and a 2001 graduate of the William and Mary School of Law, where she won the Thurgood Marshall Award for distinguished public service.