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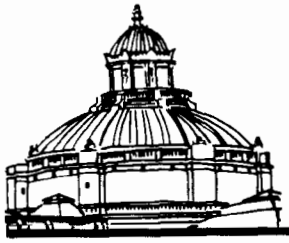
# THE UNFOLDING OF THE REAGAN ENERGY PROGRAM: THE FIRST YEAR

by
Larry B. Parker
Analyst in Energy Policy

and
Robert L. Bamberger
Analyst in Energy Policy

and
Susan R. Abbasi
Analyst in Natural Resources Policy
Environment and Natural Resources Policy Division





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# THE UNFOLDING OF THE REAGAN ENERGY PROGRAM: THE FIRST YEAR

## OVERVIEW

"Policy is a process as well as a product. It is used to refer to a process of decision-making and also to the product of that process." 1/ Both process and product have altered under the Reagan Administration; rather than developing a discrete Federal energy policy, the Reagan energy program, in contrast to that of the Carter Administration, is less comprehensive and perhaps more fragmentary. The Administration has pursued a course of transferring the locus of decision-making from the Federal Government to the States, to the private sector, and even to individuals. As stated by President Reagan, the Administration wants to remove Government intrusion in energy policy so "native American genius--not arbitrary federal policy--will be free to provide for our energy future." 2/

The absence of a comprehensive policy framework should not obscure the significance of the Reagan energy program. It is more than the abdication of energy decision-making prerogatives vested in recent years in the Federal Government. It marks a de-emphasis on energy as a problem that commands a discrete policy, and a determination that energy policy shall instead be servant to broader economic objectives and philosophies.

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1/ Wildavsky, Aaron. Speaking Truth to Power: The Art and Craft of Policy Analysis. Boston: Little, Brown and Company, 1979. p. 387.

2/ President Reagan. Nuclear Policy Statement. October 8, 1981.

This departure from the energy policy articulated by the Carter Administration reflects an economic philosophy that reaches into many areas of Government activity. If so, one should weigh the consistency of policy and budgetary decisions with those principles. Through such an assessment, other objectives which may also be governing the Reagan energy policy can be identified.

ENERGY POLICY AS PHILOSOPHY: THE NATIONAL ENERGY POLICY PLAN (NEP III)

In July 1981, the Reagan Administration unveiled its national energy plan. Required by Congress every two years, many had hoped that NEP III would provide the country and the Congress with specifics regarding the Administration's view towards issues such as natural gas decontrol, the clean air act, and emergency preparedness. However, rather than outline a plan of legislative action, the Administration's "Securing America's Energy Future: The National Energy Policy Plan" (hereafter referred to as NEP-III) is a statement of economic philosophy:

> The Administration's reformulation of policies affecting energy is part of the President's comprehensive Program for Economic Recovery, which includes elimination of excessive Federal spending and taxes, regulatory relief, and a sound monetary policy. When fully implemented, the Economic Recovery Program will release the strength of the private sector and ensure a vigorous economic climate in which the Nation's problems, including energy problems, will be solved primarily by the American people themselves--consumers, workers, managers, inventors, and investors. 3/

The energy problem has been characterized as an interlocking network of contradictory concerns, including national security, the economy, equity and, resource conservation and the environment. Previous administrations have presented energy "packages" designed to meet the objective of reducing oil imports, but with "due" concern for the other facets of energy policy. For example, in NEP I, President Carter delineated principles which established the context for his energy policy. These included:

1. Healthy economic growth must continue.
2. National policies for the protection of the environment must be maintained.

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3/ U.S. Department of Energy. "Securing America's Energy Future: The National Energy Policy Plan." page 3.

3. The United States must reduce its vulnerability to potentially devastating supply interruptions.

4. The United States must solve its energy problems in a manner that is equitable to all regions, sectors and income groups. 4/

The Reagan Administration approaches energy policy from an economic perspective, deemphasizing energy as an special or unique issue requiring special consideration. This deemphasis on energy policy is manifested by a reduced role for the Federal Government. As stated in NEP III:

> Public spending for energy-related purposes is secondary to ensuring that the private sector can respond to market realities. Even then, Federal spending should be considered only in those promising areas of energy production and use where the private sector is unlikely to invest....[U]sing public funds to subsidize either domestic energy production or conservation buys little additional security and only diverts capital, workers, and initiative from uses that contribute more to society and the economy. 5/

Unlike the Carter Administration, the Reagan Administration does not see the role of Government as designing an "energy future", balancing competing interests, or leading the country towards a energy transition. As stated in NEP III:

> Quantitative levels for the production, the consumption, or even the importation of energy in its various forms are not objectives in themselves. The American economy will choose the energy consumption for a strong, productive, and secure society in the year 2000 whether it be 80 quads or 100 quads or 120 quads of energy annually....Fundamentally, however, the best guarantee of maintaining a wholesome balance among competing interests in regards to energy lies in allowing the American people themselves to make free and fully informed choices. 6/

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4/ Executive Office of the President, Energy Policy and Planning. The National Energy Plan. pages 26-27.

5/ Department of Energy. Securing America's Energy Future: The National Energy Policy Plan. pages 3-4.

6/ Department of Energy. Securing America's Energy Future: The National Energy Policy Plan. pages 3-4.

This move to deemphasize energy as a policy issue and Government's involvement with the issue is a fundamental change from energy policies of the recent past. The Arab oil embargo of 1973 focused national attention on developing an explicit Federal energy policy. Oil shortages during the summer of 1973 prompted allusions in public statements by President Nixon to energy "self-sufficiency," a concept elevated to program status as "Energy Independence" after the onset of the Arab oil embargo.

> Let us set as our national goal in the spirit of Apollo, with the determination of the Manhattan Project, that by the end of this decade we will have developed the potential to meet our own energy neeeds without depending on any foreign energy sources. 7/

In a subsequent radio address on the energy situation, President Nixon concluded by saying that "where energy is concerned, we, the American people, shall be the sole masters of our fate." 8/

The policy response included the establishment of emergency authorities to address immediate shortages, and the infusion of Federal money into longer-term research and development. The year 1974 was a banner one for research and development: for solar heating and cooling (P.L. 93-473), geothermal energy (P.L. 93-410), electric and hybrid vehicle research (P.L. 94-413), among others.

Federal spending for alternative energy research and development increased in subsequent years. Price and allocation controls remained on crude oil and some petroleum products, particularly gasoline; price controls remained on natural gas. Shortly before leaving office, President Ford characterized the continuing dispute over energy policy during his term as resulting from "differing

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7/ Nixon, President Richard M. Address on the Energy Emergency. November 7, 1973. Appearing in: U.S. Congress. Committee on Energy and Natural Resources. Executive Energy Documents. July 1978, Publication No. 95-114. 95th Congress, 2d session. p. 86.

8/ Ibid., p. 118. Address given January 19, 1974.

views as to the appropriate role of the Federal Government." The President maintained that the primary responsibility for energy should "continue to rest with the private sector," and warned against thoughtless expansion of the Federal role. 9/

However, the National Energy Plan submitted by President Carter to Congress in April 1977, proposed to vigorously expand the Federal role in energy policy. As its first principle, the plan stated that "...the energy problem can be effectively addressed only by a Government that accepts responsibility for dealing with it comprehensively." 10/ In part, President Carter proposed to use authorities established by prior enactments. However, the National Energy Act extended Federal authorities to govern energy decision-making by industry, institutions and individuals in several areas. The Powerplant and Industrial Fuel Use Act (P.L. 95-620) established authorities whereby the Federal Government can require electric powerplants and major fuel-burning installations to utilize energy sources other than natural gas or petroleum. The Natural Gas Policy Act (P.L. 95-621), while it provided for the eventual deregulation of most categories of natural gas, placed previously unregulated intrastate gas under regulation. The Energy Tax Act (P.L. 95-618) established an excise tax on the purchase of fuel-inefficient cars.

This trend and the philosophy behind it are repudiated by the Reagan approach to energy policy. Essentially, the Reagan approach is a philosophical return to the "old-time religion" that characterized energy policy before 1973. It is a return to an implicit energy policy where the locus

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9/ Ibid., p. 356.

10/ See: U.S. Congress. Committee on Energy and Natural Resources. The President's Energy Program. May 1977. Publication No. 95-16. p. 96.

of decision-making is vested in the private sector and in the marketplace which makes all decisions governing which fuels, in what volume, in what mix, at what price, and for what purposes are produced. The role of the Federal Government in energy is distinctly subordinate to decision-making in the private sector. 11/

The Reagan economic philosophy as applied to energy policy and explained in NEP III raises several significant policy issues. Among the more important ones presented in NEP III are the following:

1. Reducing oil imports should not be the driving force for U.S. energy policy. The needs of the economy as dictated by the marketplace should control the importation of oil as any other decision would be economically inefficient.

2. Energy consumption has no normative content. Whether the country choses to use 80, 100, or 120 quads a year in energy is irrelevent as long as the economy is sound.

3. The principal role of the federal government is to increase energy supply through leasing, promoting nuclear power, economic incentives, long-term R and D, and reducing regulation.

4. Equity is not a concern of energy policy. Although the poor may suffer, distorting the marketplace will hinder an economic recovery program designed to help all Americans, including the poor.

5. Government planning is counterproductive to energy policy. Government does not have the insight or knowledge to guide energy policy. Policy should be determined by the marketplace in response to circumstances as they arise.

Reducing oil imports has been a continuing theme in energy policy since the 1973 oil embargo. From "Project Independence" to the "Moral Equivalent of War," Presidents have used the national security aspect of energy policy to justify their proposed energy policies. Most recently, the national

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11/ U.S. Congress. House Committees on Interior and Insular Affairs and Interstate and Foreign Commerce. Gulick, Frances A., David Gushee, and Warren H. Donnelly. Overview Commentary on the President's National Energy Plan. November 1977. p. 16.

security argument was employed to enact an $88 billion synthetic fuels effort. 12/ As stated by the Congress in the Energy Security Act:

> The purpose of this title, and the amendments made by this title, are to utilize to the fullest extent the constitutional powers of the Congress to improve the Nation's balance of payments, reduce the threat of economic disruption from oil supply interruptions and increase the Nation's security by reducing its dependence upon imported oil. 13/

The Reagan Administration feels that such an all-out effort to reduce oil imports is economically inefficient and will not significantly decrease U.S vulnerability to oil disruptions. Reducing oil imports "at any cost is not a major criterion for the Nation's energy security and economic health." 14/ To the extent that imported oil is overpriced vis-a-vis domestic alternatives, it will be replaced by market forces in search of the cheapest form of energy. The Administration attributes part of the current downward movement in oil imports to the economy making these types of adjustments. During disruptions disruptions, primary reliance should remain with the market to allocate supply supplemented by the Strategic Petroleum Reserve and private stocks.

Such a philosophy disturbs some who feel the approach ignores the complexity of the market and historic consumer behavior. Critics of a strict free market approach argue that social and institutional variables can frustrate the selection of economically efficient alternatives. For example, the Administration believes that market economics is sufficient to spur conservation. Yet, in situations where individuals rent their residences

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12/ For a discussion of the debate on title 1 of the Energy Security Act, see Parker, Larry and Paul Rothberg. In Energy Initiatives of the 96th Congress (forthcoming committee print).

13/ P.L. 96-294, sec 100(b)(1).

14/ Department of Energy. Securing America's Energy Future: The National Energy Policy Plan, page 2.

or commercial space, neither the tenant nor the building owner may have an incentive to save energy. Tenants have no incentive to make energy conservation improvements on buildings they do not own, and owners have little incentive to make improvements if the tenants are paying the bill. 15/

A second concern of critics is that an energy policy which bases decisions about oil consumption primarily on the basis of economic "rationality" may ignore interests of national security in reducing the nation's dependence upon imported petroleum. This concern is heightened by the near-term stabilization of oil prices, and the otherwise welcome prospect that OPEC may soon agree upon a long-term pricing strategy that will lend some predictability to prices for several years to come. If price stabilizes over a period of time as it did in the mid-to-late 1970s, consumers will become less sensitive to the need to conserve oil and less inclined to convert from oil to other fuels.

Differences in energy policy between the Reagan and Carter Administrations are also explained by a conflict in social values and outlook. During his Administration, President Carter hinted that many Americans were profligate and consumed more energy than was necessary to maintain comfort and a reasonable quality of life. What was novel in President Carter's pronouncement was its "ascetic" flavor. The Carter Administration suggested that Americans were to lower their expectations and consume less energy--not only because it would save money, but because the Nation would be morally

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15/ For other institutional barriers, see Carl Blumstein, "Social and Institutional Barriers to Energy Conservation." In Forecast--Volume II: Energy Conservation in Cities, by the Congressional Research Service, December 1978, committee print for the House Committee on Science and Technology, 95th Congress, 2nd session.

richer for doing so. In his address to the Nation on April 18, 1977, President Carter observed, "I think most of you realize that a policy which does not ask for changes or sacrifices would not be an effective policy at this late date....I have faith that meeting this challenge will make our own lives even richer." 16/

The Reagan Administration rejects this moralistic view of energy consumption. Energy consumption per se has no normative content. Rather, a growing economy is the object of Administration policy. Economic growth is the social value of concern to the Reagan Administration, not energy consumption. 17/ To the extent energy facilitates economic growth, it is important. But the *economy* should choose the appropriate consumption level, not Government.

Critics of this approach to energy consumption attack either the social value on which it is based (economic growth), or the method of execution (market economics), or both. Nurtured by the affluence and the anticompetitive values of the 1960s, offshoots of the environmental movement have expanded their concern for growth to a broad spectrum of human activities: population, energy and resource consumption, and even economic growth as it is currently measured. The finite limits of global resources and environmental equilibrium are perceived to be dangerously near by these "limits to growth" advocates. Hence, they feel the country should de-emphasize a materialistic definition of life as exemplified by economic growth, and concern itself with other human and environmental issues.

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16/ Executive Energy Documents, op. cit., p. 391.

17/ For a discussion of social values and energy policy, see Behrens, Carl. "National Goals and Social Values in Energy Policy." In U.S. Energy Outlook: A Demand Perspective for the Eighties. July 1981, committee print for the House Committee on Energy and Commerce.

Proponents of the limits to growth approach, as well as other critics of traditional energy sources, 18/ attack the so-called free market approach as naive, noting that the market is biased in favor of traditional fuels through Government subsides and the financial markets. As stated by S. David Freeman, Director of TVA:

> As it is, market forces are heavily tilted in favor of energy production and against conservation.... The production organizations have access to capital on terms that would be the envy of the average energy consumer. Investments in electric power plants, coal mines, and petroleum production are traditionally made in large amounts, in the expectation of a long-term payout. And these organizations are not in the business of conserving energy. The oil companies now talk about conserving, but they are in the business of selling petroleum. As for the utilities, they until very recently were forbidden to invest in energy conserving equipment for their consumers, even though it has been in their economic interest to do so for the better part of a decade....The market bias against conservation is even more pronounced on the consuming end. 19/

However, the emphasis of the new administration is on energy production. As stated in NEP III: "Sound public [energy] policies must be based on recognition of the Government's and the private sector's respective roles in energy production. The Federal Government's most direct impact on America's energy future arises from its position as the steward of the Outer Continental Shelf and ... publicly controlled land,...."20/ To assist private enterprise in exploiting the country's natural resources, the Reagan Administration is committed to reducing regulation and facilitating access to public lands. Also,

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18/ Some critics of traditional energy sources, such as Amory B. Lovins, have denied their allegiance to the limits to growth thesis. For a discussion of the soft path and its relationship to the limits to growth thesis, see Behrens, op. cit., p. 455.

19/ Statement of S. David Freeman, Director, Tennesse Valley Authority, before the Subcommittee on Energy, Nuclear Proliferation and Government Processes, Committee on Governmental Affairs, U.S. Senate. July 21, 1981.

20/ Department of Energy. Securing America's Energy Future: The National Energy Policy Plan. page 1.

the Administration intends to revitalize the nuclear option, including the breeder, along with emphasis on long-term, high-risk, research and development.

Critics believe that the emphasis on energy supply is misplaced: that conservation is the quickest and cheapest way to meet the country's energy problem. It is conservation, not increased energy supply, which has brought oil imports down to their current level, and proponents of conservation believe that active Federal support for conservation could accelerate this trend.

A second concern of conservation proponents is equity. The poor face immmediate problems regarding energy costs for essential needs such as heating and transportation. This problem is exacerbated by the Reagan Administration's policy of using prices to spur conservation. Also, the Administration's primary device to encourage conservation--tax credits--are of little use to poor people. Hence, an active Government role in protecting low income families from rising energy prices is considered essential.

The Administration agrees that the poor may suffer disproportionately because of rising energy prices. However, the Administration believes that the best way to help the poor is to restore the economy through free markets and the private sector. Therefore, the Administration feels the energy markets should not be distorted to assist low-income groups. Rather, their needs should be addressed by the Administration's overall social policy, particularly through block grants to the States.

This reliance on the market to direct policy is the backbone of the Reagan approach to energy policy. As stated in NEP III:

> Computers cannot gauge human response to future situations with precision. This is the key explanation of why projections of future

> energy consumption and production have been so often wrong, although there has also been a general bias against market flexibility in the assumptions of many models. Increased reliance on market decisions offers a continuing national referendum which is a far better means of charting the Nation's energy path than stubborn reliance on government dictates or on a combination of subsidies and regulations. 21/

This perception dictates minimum Federal involvement in energy policy-making, a distinguishing characteristic of energy policy before the oil embargo of 1973-74. In its reassertion of this principle, the Reagan Administration has repudiated the direction which energy policy has taken since the embargo. To the Reagan Administration, the sweeping changes in energy policy, price and politics subsequent to the embargo did not alter the appropriateness of the marketplace, with minimal Federal intervention, to address national energy problems. Indeed, the Reagan Administration, often citing the experience with petroleum price and allocation regulations, has strongly argued that the centralization of energy decision-making within the Federal Government compounded the problem.

The discussion below outlines the new Administration's approach to several major energy sources and policy issues, the initiatives presented by the Administration, congressional response, and an assessment.

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21/ Department of Energy. Securing America's Energy Future: The National Energy Policy Plan. July, 1981. page 2.

OIL

Within days of its accession to power, the Reagan Administration, meeting the promise of its frequent campaign vow to reduce Federal energy regulation, exempted gasoline and crude oil from price and allocation controls effective January 28, 1981. The decontrol action was an early bellwether of the Administration's economic and political philosophy. As is expressed in NEP-III, the marketplace "offers a continuing national referendum" on charting the Nation's energy future, and is far preferable to "stubborn reliance on government dictates or...subsidies and regulations." 22/

The role of markets captures only part of the significance of decontrol. The decision to decontrol oil symbolizes the Administration's fundamental premise that energy is no longer a discrete problem, but a policy issue to be treated as part of an overall economic recovery program. "The challenge ahead," notes NEP-III, "is to provide a healthy economy and policy environment that enables....rational energy production and consumption decisions..." 23/ The possible dismantling of the Department of Energy (not to mention the comparatively modest length of NEP-III itself) is a further reflection of the re-ordering of energy's position in the policy hierarchy.

Prior to the decontrol decision, oil decontrol was typically perceived as a policy which would promote more efficient use of petroleum and lower its consumption, even if one challenged claims made for the increased production promised by proponents of decontrol. Indeed, the Reagan Administration holds optimistic expectations from the increased investment

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22/ NEP-III, op. cit., p. 1.

23/ Ibid.

within the exploration, production, and refining segments of the industry which the Administration suggests that decontrol has encouraged.

However, decontrol is not the sole feature of the Administration's oil pricing policy. The Administration strongly notes in NEP-III that the decision to no longer subsidize petroleum consumption must be coupled with a decision to not subsidize its substitutes.

By subsidizing energy costs through price controls, energy policy was social policy, the Administration reasons. By supporting research and development in demonstrated technologies for petroleum substitutes that were not economically competitive, energy policy incurred costs to the Government incommensurate with the national security benefits on which the expenditures have been justified. Both policies, the Reagan Administration contends, were inconsistent with rational economic policy.

Rational market decisions should reflect "the true value, in every sense, of all the Nation's resources," the Administration notes in NEP-III. Imported oil may be less expensive in some instances than substitute fuels, and while

> efficient displacement of imported oil is an important objective, achieving a low level of U.S. oil imports at any cost is not a major criterion for the Nation's energy security and economic health. 24/
> (emphasis in original)

It was error to subsidize the price of imported petroleum, the Reagan Administration argues; it would be equally inappropriate "if market forces were distorted through indiscriminate subsidies for alternatives that cost more than imported oil." The key word is "indiscriminate"--instances

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24/ Ibid., p. 2.

in which the potential alternatives "offer no short-term to medium likelihood of being economically competitive."

In short, the Administration's oil pricing policy is more than just a reassertion of markets. Oil pricing policy aptly reflects the manner in which the Administration has de-emphasized energy policy, asserting that energy policy should serve economic goals instead of subordinating economic objectives to energy policy, or masking social welfare and defense policies as energy policies.

EMERGENCY PREPAREDNESS

On September 30, 1981, the authority delegated by Congress to the President in the Emergency Petroleum Allocation Act of 1973 to impose comprehensive price and allocation controls expired. During the first session of the 97th Congress, a number of bills were introduced to restore this authority, provide for dispersal of the Strategic Petroleum Reserve, or institute a revenue recycling mechanism for insulating consumers from the economic shocks that would likely accompany a shortage of petroleum products.

The Administration has expressed unqualified opposition to the extension of price and allocation controls, and any Federal intervention in the marketplace during petroleum shortages. In the event of shortage, the Administration proposes: (1) maximum reliance on the free market to determine the price and allocation of energy supplies, and (2) full participation in the international oil-sharing program of the International Energy Agency. In the meantime, the Administration supports rapid growth of the Strategic Petroleum Reserve, and seeking measures to encourage stock buildups in the private sector during times when supply is secure.

The Administration believes there is no necessity for or practicality in articulating an emergency response plan in advance of a disruption; the appropriate action will be undertaken as warranted should an emergency occur. The Administration is opposed to controls, and contends that the mere establishement of authority to impose them sends an inappropriate signal to the private sector that it may possibly count upon Federal intervention to protect its access to crude or products during a shortage.

While it appears that most Members of Congress believe that price and allocation controls were largely ineffective and inefficient, their opposition

to controls is not so absolute as the Administration's. The major congressional initiative has been S. 1503, the Standby Petroleum Allocation Act of 1981, introduced by Senator McClure, and passed by the Senate on October 29, 1981.

Recognizing that there would be little hope that the President would sign a bill "loaded" with mandatory directives to the President or provisions establishing priority allocation to certain users, the bill was intended simply to provide the President with discretionary authority to allocate crude and products in the event of a serious shortfall.

Nonetheless, the bill was besieged in committee with a number of admendments, and to forestall lengthy and acrimonious debate, the committee agreed to incorporate language from the Emergency Petroleum Allocation Act of 1973 (EPAA) establishing that the standby regulations would provide for the protection of certain users and uses of crude and petroleum products. The legislation, as passed by the Senate, would permit the President to implement standby crude or product allocation regulations in the event of a serious shortage or to meet U.S. obligations to the International Energy Agency. The regulations would be in effect ninety days, if neither House of Congress disapproves, and could be extended another sixty days without congressional review. Price controls are provided for if necessary to achieve the objectives of the allocation regulations. The bill also includes language that preserves the Federal prerogative to determine when, and in what manner, petroleum may be subject to price and allocation controls, but provides that areas of regulatory activity not assumed by the Federal Government during an emergency could be undertaken by the States. Comparable legislation has been considered in the House.

A confrontation between the Administration and Congress may be looming, centering around the Administration's most basic faith in free markets and decentralization. Many in Congress appear to agree with the Administration that one cannot make specific provisions for shortages of unknown duration and character, but are skeptical that the free market would function swiftly enough under all circumstances to provide for critical needs. In introducing S. 1503, Senator McClure observed that "we cannot resposibily be dependent on anything less than full preparation after expiration of EPAA," and that the Administration must be fully prepared "should federal action become necessary to supplement the market mechanism."

However, the proposed bills do not require the Administration to specify the precise actions to be taken under particular circumstances. The standby regulations that the Administration would be required to develop might be imprecisely worded while still complying with the requirements of either the House or Senate legislation. Development of implementing regulations could be postponed until the onset of an actual emergency, preserving the latitude upon which the Administration insists. Given these considerations, and the likely strength of the congressional consensus, the Administration may decide this issue is not worth the fight--and possible defeat.

NATURAL GAS

Not long after decontrolling petroleum, the Reagan Administration hinted its intention to seek early decontrol of natural gas. The President's Energy Policy Task Force report, prepared and released in December 1980, urged "phased decontrol...notwithstanding present 'decontrol' legislation," a reference to the Natural Gas Policy Act.

The text on natural gas, which is one of the shortest passages in the fuel-specific section of NEP-III observes that important premises of the Natural Gas Policy Act (P.L. 95-621) have been "overturned" by subsequent events: (1) the price of oil has more than doubled beyond what it was projected to rise to in 1985 by the NGPA; and (2) because of this widening disparity, natural gas resources are not being properly exploited because there is less incentive to explore for gas than for oil.

As a matter of economic principle for the Administration, decontrol of natural gas should be a straightforward matter. But politically--and even economically--it is not. The deliberation over the Natural Gas Policy Act of 1978 was exhausting, sustained on the hope that Congress would not need to address the issue for several years. The Administration and Members of Congress with special interest in natural gas decontrol recognize how little appetite either party would have for a major confrontation. It can be expected, then, that any major proposal introduced in the 97th Congress will be further along the path of consensus than was the Natural Gas Policy Act in its original form.

If consistent with the economic philosophy of the Reagan Administration, decontrol would be inconsistent with its economic policy. Though

the impact would be difficult to calculate and would vary with the specifics of policy, decontrol would certainly contribute to inflation and would offset some of the tax reductions that were described as fundamental to the Administration's program. Most importantly, any significant decontrol measure might not survive congressional consideration without passage of a windfall profits tax, which the President, in a now celebrated note to Representative Glenn English has said he would oppose. Windfall profits taxes are, to the Administration, archetypical instances of "burdensome" Federal policies which discourage private sector initiative. However, the Reagan Administration has been held captive by the windfall profits tax on oil--for obvious political reasons--made somewhat less distasteful by the helpful budget-balancing revenues it provides. Some speculate that natural gas decontrol accompanied by a windfall profits tax might commend itself to the Administration for the same reason, but the initiative for a windfall profits tax would clearly be left to the Congress.

For the moment, natural gas decontrol continues to be the object of various studies, position papers and discussion. The debate will center about determining what categories (and, therefore, what volumes) of gas should be decontrolled; and whether some categories of gas are decontrolled immediately or subject to phased decontrol. If the latter, an additional issue will be deciding what the "target" uncontrolled price should be.

One concern about decontrolling gas is that rising gas prices could prompt industrial and utility users to switch to oil. This would be inconsistent with the avowed national policy goal of reducing oil imports (albeit, not at any cost); the equivalent cost for residual fuel oil has

been suggested as a possible "target" price to avoid oil displacing gas consumption.

The President's Cabinet Council on Natural Resources and the Environment was reportedly pressing for the President to reach some decision on accelerating gas price decontrol by late September or early October 1981, but preoccupation with the second round of budget cuts and the proposed dismantling of the Department of Energy has postponed release of the Administration's proposal until early 1982. Enactment of legislation to accelerate natural gas decontrol may be a strong possibility in 1982. Only the particulars remain to be worked out, an "only" premised upon hopes by Congress, the Administration and the industry that achieveing consensus will be less painful the second time around.

COAL

The Administration appears confident that market conditions favor coal development provided the Government gets out of the way. This confidence is resulting in new proposals both to promote production of coal and removing existing direct subsidies and regulations which promote production. The Administration is acting to encourage exploration and production on Federal lands, to change the Clean Air Act, and to reduce Federal regulations of land reclamation. The Administration also has succeeded in repealing the "off gas" provision of the Fuel Use Act, and has sought a reduction in coal Research and Development and synthetic fuels efforts.

This more laissez-faire attitude towards coal differs from that of the Carter Administration, which set ambitious production goals for coal-one billion tons annually by 1985. As proposed by President Carter, the expansion was to be induced by a combination of tax and regulatory measures. 25/ Taxes would have been used to raise the cost of industrial use of oil and gas and encourage conversion to coal. A regulatory program was enacted to prohibit new oil- and natural gas-fired boilers with some exceptions, and to phase out existing natural gas boilers by 1990. Also, strict environmental regulations would have been enacted to protect the air and reclaim disrupted land.

The Administration hopes to replace this partially enacted regulatory system with a market system to encourage coal. The decision to decontrol oil raises the cost of one competitor to coal--residual fuel oil. However, natural gas is still under controls; complete decontrol would require congressional action. With the repeal of the "off gas" provision of the Fuel Use Act,

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25/ See National Energy Plan, Executive Office of the President, Energy Policy and Planning, 1977.

industrial consumption of natural gas may increase at the expense of coal unless natural gas decontrol occurs in the near future or environmental regulations are altered.

To improve coal's attractiveness to private industry, the Administration is recommending changes in the Federal reclamation laws and the Clean Air Act. Believing the Office of Surface Mining (OSM) has promulgated regulations far in excess of the requirements of the Surface Mining Control and Reclamation Act, Secretary Watt has recommended major changes in the Federal guidelines for surface reclamation. The crux of the new proposals involves replacing the current "design standards" with "performance standards" which the States would enforce. The purpose is to increase flexibility in restoring disturbed lands and return primary responsibility for enforcement back to the States.

However, the Administration may be trading flexibility for uncertainty. Although rigid and detailed, the current regulations have been fully tested in court and provide a known regulatory regime. New proposals, particularly of the variety the Administration is proposing, would probably face court challenges both on substantive grounds and on the legality of Secretary Watt's intepretation of the Surface Mining Control and Reclamation Act. Such changes would also invoke some Congressional opposition. This legal and legislative turmoil may arrive just as coal developers are becoming familiar to the current rules, and delay the supply-side response the Administration is trying to encourage.

The Administration also has indicated it wishes to relax environmental regulation. In particular, the Administration has suggested elimination of the "technology standard" mandating a percentage reduction of sulfur dioxide in power plants regardless of the emission level. In its place the Administration would impose a "performance standard" mandating an upper limit on permissible

emission levels. This would provide plant developers flexibility in meeting the standard, either through low-sulfur coal, or emission control technology.

A performance standard would encourage the use of western low-sulfur coal as an less expensive alternative to scrubbers in meeting a performance standard. Generally, western coal-producing States are in a boom situation with their low-sulfur coal. However, because of the States' small populations, the technology involved (strip-mining), and the rapid nature of the growth, these States are struggling to control the situation. This contrasts with some eastern States which currently have idle mining capacity and unemployment problems. A performance standard would increase the competitive advantage western States have in the midwest and southwest, to the detriment of eastern coal States. Such a situation could arguably exacerbate the growth-related problems of western States, and the contraction problems of eastern States.

Also, depending on the emission limit set, a performance standard might increase the aggregate amount of SO2 emitted. Such an increase, or the possibility of an increase, could strain relations with Canada regarding acid rain. Power plant emissions are generally regarded as a major contributor to acid rain 26/ and the Canadian Government feels the United States must act to control such emissions which are affecting parts of eastern Canada. How the Canadians would perceive changes in the Clean Air Act is unclear.

In summary, the focus of the Administration's action in coal is to provide a more flexible regulatory environment for coal exploitation and development. However, such efforts will not provide relief to the coal industry in the short term, and may in fact increase regulatory uncertainty.

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26/ See National Research Council, Committee on the Atmosphere and Biosphere's report on the burning of fossil fuels, September 1981.

SYNTHETIC FUELS DEVELOPMENT

During the debate on the Energy Security Act (P.L. 96-294), the principal argument of proponents for Government assistance to synthetic fuels efforts was national security. The potential economic inefficiency of investing in synthetic fuels plants as opposed to other sources was overridden during debate by the security issue.

For the Administration, synthetic fuels represent a dilemma. Although synthetic fuels could assist in reducing oil imports, the uncertainties concerning their development may deter private industry from taking the risks without Government assistance. Also, it may be more economically efficient to put that money into other, more near-term, cost-effective technologies. In NEP III, the Administration states that oil imports should be reduced only to the extent that it is economic to do so. With the philosophy of the Administration, private industry is the appropriate sector to make this decision, not the Government.

The Administration has proposed shifting the focus of Government synfuels programs to the U.S. Synthetic Fuels Corporation. Such a move is designed to increase the influence of market forces in synthetic fuel development, while assisting industry in coping with the expensive learning process that development of synthetic fuels will require. In line with this belief, the Administration called for the elimination of the DOE demostration programs, including SRC I and SRC II (the latter being built under an international agreement with West Germany and Japan). Also, the Administration recommended drastic reductions in synthetic fuels research and development. The proposed FY82 budget cut R and D for coal liquefaction from $886.3 million to $105.2 million, surface gasification from $216.4 million to $53.4 million, and in situ coal gasification from $10.5 million to $8.3 million.

NUCLEAR

After 4 years of being considered an energy source of "last resort" by the Carter Administration, nuclear power is now regarded as a potentially large and long-term contributor to the national energy mix. The Carter Administration looked on uranium as an important fuel in the near term, but viewed it as a transition to long-term renewable energy sources. The Reagan Administration, however, views fission as an "essentially inexhaustible energy supply." As a result, the development and demonstration of breeder reactor technology, which the Carter Administration had deferred and deemphasized, is considered essential. The total FY82 Reagan nuclear budget request was $1.054 million, compared with $813 million from the previous Administration. The primary source of this increase was the decision to fund the Clinch River Breeder Reactor project (CRBR), which President Carter omitted in his FY82 request.

It is the Reagan Administration's decision to fund Clinch River which has raised the most controversy in the Congress regarding nuclear policy. Noting the Administration's decision to recommend elimination of solar, alcohol, and coal synthetic fuels demonstration programs by stating such projects should be developed by private enterprise, opponents have suggested the same rationale be consistently applied to Clinch River. However, the Administration decided that breeder development was "outside the range of normal industry risk-taking" and thus merits Government support. As with the coal synthetic fuels demonstration program, the controversy over Clinch River illustrates the apparently ambiguous nature of the "long-term, high risk" criteria employed by the Administration in making research and development decisions, and the ability of various

other considerations besides market viability to enter into research and development policy decisons.

A more straightforward question of market viability involved the Barnwell Fuel Reprocessing Facility. In a decision consistent with the proven nature of reprocessing technology, the Administration recommended no funds for Barnwell, while lifting the Carter Administration's ban on commercial reprocessing. However, given the current ample supply of uranium, the private sector has shown little interest in reprocessing unless the Federal Government can guarantee a market for the plutonium.

The Administration's support for nuclear is evident in its recently released nuclear policy statement. Besides supporting CRBR and commercial reprocessing, the Administration reiterated its support for the light-water reactor program stating: "one of the best potential sources of new electrical energy supplies in the coming decades is nuclear power." Besides protecting the various parts of the DOE fission budget from cuts, the Administration limits Federal actions favoring commercial nuclear power to two: economic recovery to "improve the climate for capital formation" through tax incentives and fiscal restraint, and elimination of "regulatory burdens." Beyond those steps, the President's nuclear statement offers a study and a report in a year on "obstacles which stand in the way of increased use of nuclear energy and steps needed to overcome them"--and an implict halt on negative rhetoric regarding nuclear safety and the dangers of nuclear proliferation.

In his policy statement, the President states:

> ...the federal government has created a regulatory environment that is forcing many utilities to rule out nuclear power as a source of new generating capacity, even when their consumers may face unnecessarily high electric rates as a result, Nuclear power has become entangled in a morass of regulations that do not enhance

safety but that do cause extensive licensing delays and economic uncertainty. 28/

However, a major cause for the delay in nuclear power plant construction is the drop in electricity demand due to increasing electricity prices coupled with a slowing economy. Future electricity demand is uncertain, leaving financially strapped utilities in a bind. Do the utilities proceed to increase capacity, assuming elecricity demand will return to historic levels? Or do they assume demand will remain restrained and rely on alternatives which may be inefficient if demand does return to historic levels? A decision to increase capacity through a nuclear or fossil fuel plant requires a significant long-term investment. If demand does not increase to ensure economic use of the added capacity, the utility still has to cover its investment. Given the current economic situation, utilities are finding this difficult to do.

The President's nuclear statement maintains that relieving regulatory burdens on the industry and providing moral support is insufficient to revitalize the nuclear option. As stated by the President: "Eliminating the regulatory problems that have burdened nuclear power will be of little use if the utility sector cannot raise the capital necessary to fund construction of new generating facilities." To improve the climate for nuclear power, the Administration believes it must improve the general economic situation. A growing economy generating increased electricity demand is considered essential to a revitalized nuclear industry. Unless the Administration's economic policies can achieve this, the Administration fears its support for the nuclear option will have limited impact.

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28/ President Reagan. Nuclear Policy Statement. October 8, 1981.

CONSERVATION

Conservation and solar energy development were primary tenets of the Carter Administration's energy policy. Support for this emphasis was evident by the public hearings on NEP III held by the Reagan Administration. As summarized by DOE, conservation was "clearly the major theme" of the Boston hearings, and speakers were "vitually unanimous" in favor of Government-supported conservation programs at the Atlanta hearings. DOE was accused of promoting synthetic fuels and nuclear while ignoring conservation. 29/

Despite these comments on the draft NEP III, the final NEP III contains little regarding conservation. Less than one-tenth of the report discusses conservation's role in the Reagan energy policy. The report states the Administration's belief that rising energy costs will be sufficient incentive to promote conservation without active Government assistance. Price and tax credits are the mechanisms the Administration believes will promote conservation, not Government programs.

The Administration recognizes that price and tax credit mechanisms will not help the poor cope with higher energy prices, but feels such suffering must be considered in the context of overall social and economic policy, not energy policy. The Reagan Administration believes a growing economy is the best way to help the poor--"a rising tide which will raise all the boats." However, the time at which the tide will come and its height are unknown. Given the Reagan Administration's cuts in energy programs to assist low income families, the answer to these questions are critical in determining how much suffering the poor will have to endure.

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29/ See Capital Energy Letter, May 4, 1981. p. 3.

Consisted with this philosophy of limited Government assistance for conservation, the Reagan Administration has recommended significant reductions in all conservation programs; reductions to which the Congress has partially agreed. All three categories of conservation programs--research and development regulation, and grant programs--have been reduced. Reflecting the philosophy that Government research and development should focus on longterm needs, the Administration recommended termination of several research and development projects on the premise they should stand the test of market viability without Government assistance. These included urban waste, consumer products, advanced automotive engine design, and industrial processes projects. In the Reconciliation Act, the Congress agreed to reduce but not terminate these research and development programs. The Congress doubled the Administration request for conservation research and development programs from $86 million to $182 million. However, this is still a significant decrease from the 1981 funding level of $290 million.

Regulatory programs for building energy performance standards, appliance efficiency standards, and utility conservation services, are not great burdens on the DOE budget. However, reflecting its belief in deregulation, the Administration called for the termination of these programs, arguing that these programs impose too great a burden on private industry. In the Reconciliation Act, the Congress authorized $40 million to continue these programs. However, the Congress also agreed to make the proposed building energy performance standards voluntary rather than mandatory.

Finally, DOE conservation grant programs to States and local communities have also been cut. In his original budget request, the President recommended terminating funding for State energy offices and outreach programs, reducing

support for the schools and hospitals program ($100 million), and incorporating DOE's weatherization program for low-income people into the Department of Housing and Urban Development community development block grant program. These recommendations met with significant resistance in the Congress which wished to retain funding for these programs. In the Reconciliation Act, the Congress authorized $336 million to fund these various programs and recommended that they all continue.

In recognition of this congressional support, the Administration in July 1981 backtracked from its original position. Faced with an attempt to reauthorized all DOE catagorical grant programs (S.1166), the Administration introduced a counterproposal entitled the "State and Local Energy Block Grant Act of 1981." (S. 1544). As stated by OMB Director Stockman:

> ...Under these circumstances,[reconciliation funding for grant programs] in a spirit of compromise, the Administration would not oppose legislation authorizing a State and Local Energy Block Grant for energy supply, conservation, and low-income weatherization activities which would repeal and replace all the existing categorical conservation grant programs, including the Residential Conservation Service, and for which funding would be authorized at a level not in excess of $200 million per year. 30/

This proposal may not satisfy supporters of Government conservation programs because of its inclusion of energy supply into the areas eligible for funding, the funding level which is one-half that suggested for S. 1166, and the refusal of the Administration to support appropriations for it.

In summary, the President has achieved a significant reduction in Government support for energy conservation programs, although not complete elimination of them. That he has been unable to achieve more cuts in conservation

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30 / Letter from David Stockman to Senator McClure. Printed in Congressional Record, July 30, 1981, p. S8862.

programs reflects a strong congressional consensus on the importance of conservation, and the belief that Government assistance is necessary to achieve the maximum benefits from conservation opportunities.

DEPARTMENT OF ENERGY

As the Reagan Administration has moved to reverse the direction of the Nation's energy policies, it has also rejected and proposed to dismantle the major symbol the previous Administration's energy policy--the Department of Energy (DOE). The DOE was the cornerstone of the Nation's energy policy in 1977 when it was established, and occupied a central role in the formulation and implementation of that policy throughout the Carter Administration. However, Presient Reagan campaigned on a promise to abolish it, and announced on September 24, 1981, that he would soon propose legislation to disband the Department. The intention to disband DOE was announced as one of several budget cutting and moneysaving measures; however, the move is seen by some as largely symbolic, since little money would be saved by abolishing the Department that could not be saved by simply cutting the DOE budget.

Following the Arab oil embargo of 1973, the Nation's energy problems were perceived as increasingly critical, and accordingly, higher levels of organizational focus were sought to deal with them. When DOE was established, both Congress and the President expressed confidence that the new Energy Department would be an important advancement in shaping more effective national energy policies. However, the pressures under which DOE operated in its first three and a half years of existence made the formulation of widely agreed upon policies difficult, and left DOE with few defenders. It had consistently been in the middle of contending and competing groups, and failed to fully satisfy any of its constituencies.

The absence of critical energy shortages since 1979 has contributed to the fading sense of urgency concerning the Federal role in energy. By 1980, President Carter no longer pointed with his earlier pride to the

establishment of DOE as a major accomplishment; President Reagan promised to abolish it.

In describing "the Federal role", NEP III failed to mention the Department of Energy at all, and made the Interior Department the central Federal actor. The plan stated:

> "The Federal Government's most direct impact on America's energy future arises from its poisition as the steward of the Outer Continental Shelf and of 762 million acres of publicly controlled land, one-third of the land area of the United States....The Federal role in national energy production is to bring these resources into the energy marketplace, while simultaneously protecting the environment." 31/

Finally, on September 24, 1981, President Reagan addressed the Nation on the economic recovery plan of his Administration, and proposed dismantling of the Departments of Energy and Education as a key move in reducing the size of Government. He stated:

> "...we propose to dismantle two Cabinet departments, Energy and Education. Both Secretaries are wholly in accord with this. Some of the activities in both of these departments will, of course, be continued either independently or in other areas of government....Now, we don't need an Energy Department to solve our basic energy problem. As long as we let the forces of the marketplace work without undue interference, the ingenuity of consumers, business, producers and inventors will do that for us." 32/

The Administration had indicated that a proposal to disband the Department--an action which would require an Act of Congress--would be forwarded to Congress by mid-November or early December 1981. However, few specifics about the proposal have been circulated. Discussion to date has centered

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31/ U.S. Department of Energy. Securing America's Energy Future: The National Energy Policy Plan. July, 1981. p. 1

32/ President's Address to the Nation, September 24, 1981. Statement released by the White House, p. 5.

around where the various functions previously housed in the Department of Energy would be transferred. An early Presidential decision paper indicated that only the Secretary's Office, the Economic Regulatory Administration, and certain energy conservation grant programs would be abolished outright; other programs would continue, often in reduced form, in other agencies. The programs of the Federal Energy Regulatory Commission, formerly the Federal Power Commission, were expected to revert to the old format in an independent regulatory agency; the nuclear weapons and nuclear energy research and development programs were similarly suggested for a new, independent agency, perhaps much like the old Atomic Energy Commission; other programs would be transferred to other departments, such as Interior, Commerce, Housing and Urban Development, and Transportation, or to agencies such as the National Science Foundation, or Federal Emergency Management Agency.

Although a number of reasons for dismantling the Department of Energy are offered as a rationale, the majo reason for President Reagan's interest in such a proposal is his perception that "...we don't need an Energy Department to solve our basic energy problem...the forces of the marketplace...the ingenuity of consumers, business, producers and inventors will do that for us." The Department is a symbol of a Federal role in managing energy supply and demand that President Reagan rejects. Since he would prefer to minimize the Federal role in energy affairs, he would also like to dismantle and remove the major symbol and reminder of the energy policies of his predecessor--policies that centered on Federal actions. The existence of a major Cabinet Department on energy is likely to continue attracting interest in what the Federal Government can or should do--in energy conservation, in energy research, in energy information, and in other areas. Most of these are areas where funding

has been cut back or eliminated, but the continued existence of the DOE is both a reminder that broader involvement is possible, and a magnet for new proposals in the areas the President believes should be left to the private sector.

However, those who favor retaining the Department argue that the DOE is indeed an appropriate grouping of functions of central importance to the U.S. economy and the well-being of its citizens, and should continue at a high level of visibility and concern in the Federal Government. Also, most other governments, both in the States and in other countries, have energy departments or ministries, and proponents of keeping a U.S Energy Department argue that the U.S. Government should have a similar entity to interact with these in dealing with energy issues. In addition, there is concern that in the event of a possible future energy crisis, the Energy Department would be needed, but that after disbanding it, it would be extremely difficult to re-establish it.

In general, at present there is considerable conern among chairmen of energy-related committees in Congress over a precipitous move to abolish DOE. The earlier assumption that Congress would speedily enact the necesssary legislation to disband the Department if the Administration requested it, is now more widely questioned. However, proponents of disbanding the Department have been critical of DOE for some time. The debate over keeping it or dispensing with it is likely to be lively, not only on organizational points, but as a symbol of the level of acceptance in Congress of the overall thrust of the Reagan Administration's energy program.

## CONCLUSION

The Reagan Administration's energy program represents the latest in a series of attempts to seek a philosophical base for rationalizing a national energy policy. In returning to the premise that governed energy policy before the embargo of 1973-4--minimal Federal involvement in energy decision-making--the Administration is repudiating the essence of Federal energy policies since the embargo. Essentially, the Reagan Administration is saying that the viability of the energy market mechanism was not fundamentally changed by the embargo or subsequent disruption; Government intervention in the marketplace was an inappropriate response to the problem, and more important, compounded the Nation's energy problems.

In contrast to the energy policy articulated by the previous Administration, the Reagan Administration's energy policy is governed by a philosophical return to a major reliance on market mechanisms to meet current and future developments. President Carter's National Energy Plan was premised on projections that world demand for petroleum would exceed supply in 1985, thus disrupting world markets. This lent an international context to what had been perceived as primarily a domestic issue. The Reagan program does not globalize national energy policy, nor has it been premised upon traditional decision-making methods such as cost-benefit analysis.

With the exception of Federal support for nuclear and some synthetic fuels, the Reagan energy policy is based instead upon a belief in the ability of private enterprise and the market to supply the country with sufficient and appropriate forms of energy to maintain healthy growth at prices affordable by institutions and individuals. The question that remains is whether such a system, based on market allocation, can provide the country's energy needs at prices

that are polictically equitable and economically affordable, and whether the international climate will permit the market to do so.