

# CRS Report for Congress

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## **Gasoline Prices: Issues for the 110<sup>th</sup> Congress**

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## Summary

The high price of gasoline was an important consideration during the debate on the Energy Policy Act of 2005, H.R. 6 (P.L. 109-58). As prices continued to surge, the continuing crisis renewed attention on some issues that were dropped or compromised in the debate over P.L. 109-58, as well as to a number of initiatives to reduce the impact of high prices on consumers. However, the 109<sup>th</sup> Congress adjourned after passing only one of them: a measure lifting some restrictions on oil and gas leasing in the Gulf of Mexico.

Continued high gasoline prices, and the change in leadership in the 110<sup>th</sup> Congress, put the energy issue in the forefront, and the House passed H.R. 6, the Creating Long-Term Energy Alternatives for the Nation (CLEAN Energy) Act of 2007 as part of its “100 hours” program at the beginning of the first session. President Bush, in his State of the Union speech on January 23, proposed cutting gasoline consumption by 20% in 10 years through increased fuel economy standards and use of alternative fuels. He also proposed expanding the Strategic Petroleum Reserve (SPR) to 1.5 billion barrels.

A large number of factors have combined to put pressure on gasoline prices, including increased world demand for crude oil and limited U.S. refinery capacity to supply gasoline to a growing national economy. The war and continued violence in Iraq have added uncertainty, and threats of supply disruption have added pressure, particularly to the commodity futures markets.

The gasoline price surge has stimulated much legislative activity, but without the urgency of previous energy crises. In part, this may be due to the fact that there has been no physical shortage of gasoline or lines at the pump. In addition, the expectation of former crises — that prices were destined to grow ever higher — has not been prevalent.

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## Most Recent Developments

Gasoline prices surged over \$3.00 per gallon in April 2006 and stayed there during the rest of the spring and summer. The summer driving season, and complications involving replacing the gasoline additive MTBE with ethanol, were cited by some observers as behind the latest run-up. However, July gasoline consumption reached a record-high 9.5 million barrels per day (mbd) despite the high prices. (See **Figure 3**.)

Gasoline prices declined sharply in September. (See **Figure 1**.) The end of the peak summer driving season and the lack of hurricanes threatening a repeat of the damage to the Gulf of Mexico production and refining capacity of the previous year were among the factors leading to the decline. At the end of 2006, however, gasoline prices were about 20% higher than at the beginning of the year, and 50% higher than at the beginning of 2004.

The continued high prices ensured that energy would remain on the agenda in the new Congress, and on January 18, 2007, the House passed H.R. 6, the Creating Long-Term Energy Alternatives for the Nation (CLEAN Energy) Act of 2007 as part of its “100 hours” program at the beginning of the first session. President Bush, in his State of the Union speech on January 23, proposed cutting gasoline consumption by 20% in 10 years through increased fuel economy standards and use of alternative fuels. He also proposed expanding the Strategic Petroleum Reserve (SPR) to 1.5 billion barrels.

## Background and Analysis

### Legislative Activities

The persistence of high gasoline prices has led to a broad spectrum of proposed new legislation. Despite passage of the major Energy Policy Act of 2005 (P.L. 109-58), many Members have continued to explore a variety of measures to increase supply and reduce demand in the short term, and to reduce the impact of high prices on consumers. The change in leadership in the 110<sup>th</sup> Congress is also reflected in revisiting longer-term policies that were left behind in the process of reaching agreement on P.L. 109-58.

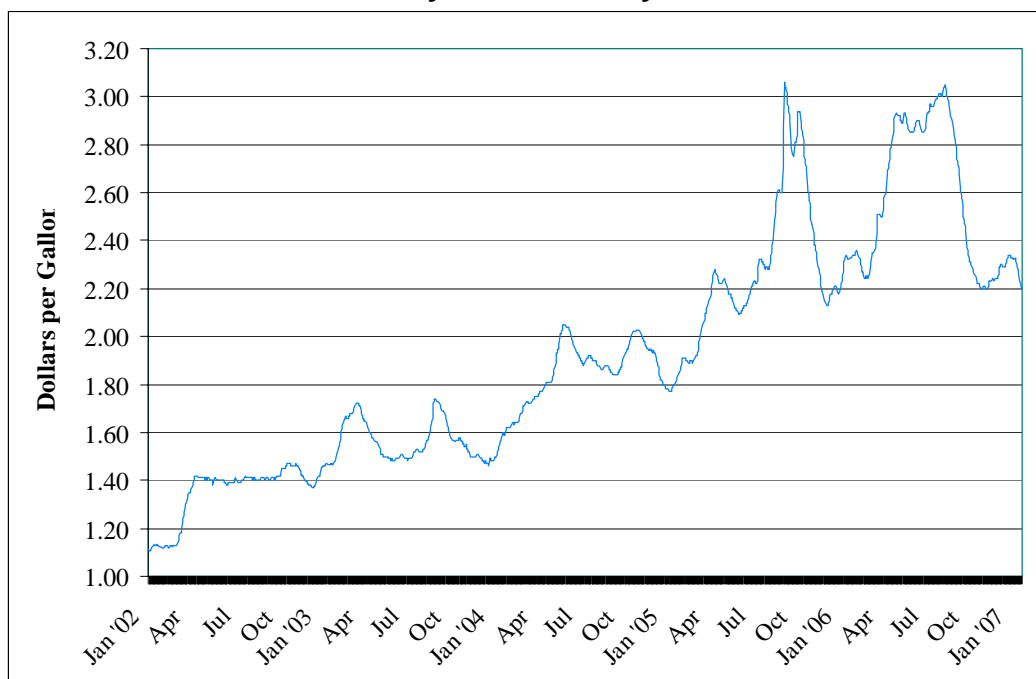
This report reviews the major legislative initiatives to deal with the gasoline price issue. To put these proposals in perspective, it first describes some of the factors that have led to the high prices of both crude oil and gasoline.

## Why Are Prices So High?

The run-up of gasoline prices that began in spring 2004 (see **Figure 1**) climaxed a period of almost five years during which gasoline prices demonstrated a great deal of regional volatility but less of an increase at the national level. In 2004, a large number of factors combined to exert pressure on gasoline prices in all parts of the country. Some of these factors have affected the price of crude oil, and others the cost of producing and marketing gasoline.

**Crude Oil Prices.** Past energy crises have demonstrated that oil is traded in a world market, in which events in remote areas affect the price of crude for almost everyone. As a result, the price of crude oil is set through the interaction of world demand and supply. Major factors in the run-up of crude oil prices have been the sharply increased consumption of imported oil by China (see **Figure 2**) and the continuing possibility of a supply disruption, either from violence or terrorism in the Middle East, or from natural disasters like Hurricanes Katrina and Rita in 2005.

**Figure 1. Average Daily Nationwide Price of Unleaded Gasoline, January 2002-January 2007**

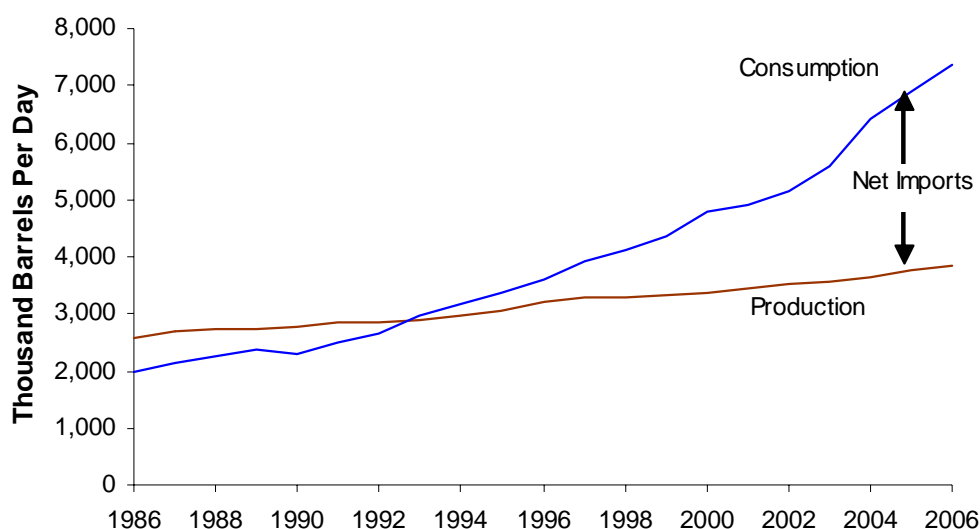


**Source:** *Daily Fuel Gauge Report*, American Automobile Association, [<http://www.fuelgaugereport.com>], compiled by CRS.

**Notes:** Prices include federal, state and local taxes. Last date above is January 19, 2007.

World demand for crude oil grew by 4% in 2004 but moderated to 1.4% in 2005 and 1.1% in 2006. It is forecast to grow by 1.7% in 2007.<sup>1</sup> World supply, at 84.5 million barrels per day in 2005, was less than 1 million barrels per day more than demand, leaving relatively little excess supply to draw on if the market was disrupted by natural or political disasters. When excess supply on the market is low, prices tend to rise and become more volatile.

**Figure 2. China's Oil Production and Consumption, 1986-2006**



**Source:** EIA, *Country Analysis Brief—China*, August 2006, at [<http://www.eia.doe.gov/emeu/cabs/China/Oil.html>].

**Note:** 2006 is January through August only.

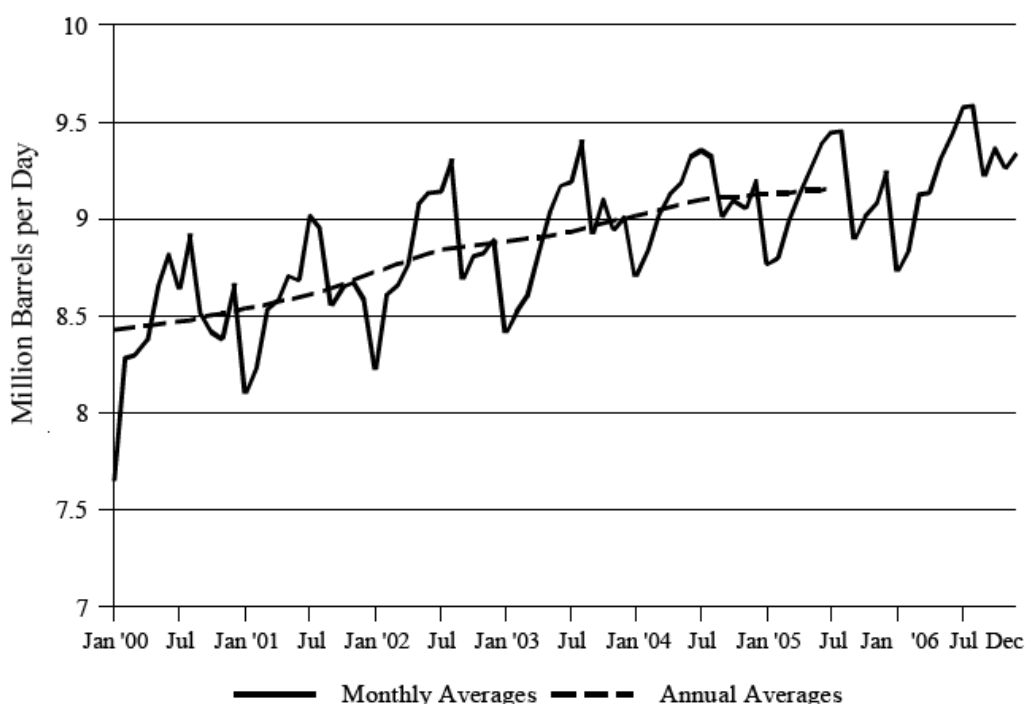
**Gasoline Prices.** Higher prices for crude oil translate directly into higher prices for gasoline. Crude oil accounts for about 54% of the cost of gasoline. Refining, distributing, and marketing account for about 30% of the cost of gasoline, and taxes account for about 16%.<sup>2</sup> Whether the crude oil a refiner processes is purchased on the open market or is produced by the oil company itself, higher costs for any element in the cost of gasoline are likely to be passed on to consumers. A number of factors have aggravated the pressure on gasoline prices, including limited refining capacity in the United States, the range of fuel blends required to meet air pollution requirements, and the mandated use of ethanol as an additive. Perhaps most important, U.S. demand for gasoline has increased as economic growth has continued (see **Figure 3**).

<sup>1</sup> International Energy Agency, *Oil Market Report*, Dec. 13, 2006, pp. 4-6.

<sup>2</sup> Energy Information Administration data based on June 2006 data and a base price of gasoline of \$2.89 per gallon. See *Gasoline & Diesel Fuel Update* [<http://www.eia.doe.gov>].

The 2004 price surge intensified discussion of energy policy and led to further calls for passage of energy legislation. However, until the climax of the Katrina disaster, the urgency of previous energy crises had been lacking. Throughout the period, U.S. gasoline consumption continued to rise. In part, this may be because although the price of gasoline in nominal terms set a record, in real terms it did not appear to be reaching the level of the Iranian crisis years of the early 1980s (see **Figure 4**); that is, until Katrina pushed it toward the \$3.00-per-gallon mark. Further, unlike the earlier crises, there was no physical shortage of gasoline and there were no lines at the pump, except in local disaster-affected areas.

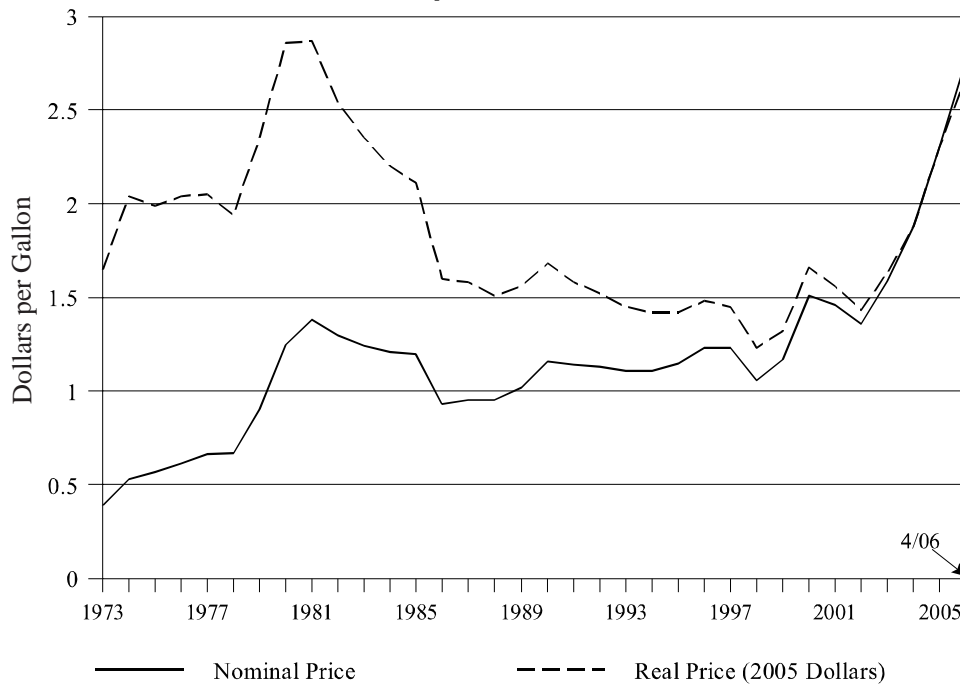
**Figure 3. U.S. Gasoline Consumption, 2000-December 2006**



**Source:** EIA, *Monthly Energy Review*, December 2006, Table 3.4, and *Weekly Petroleum Status Report*, Jan. 10, 2007, Table 10.

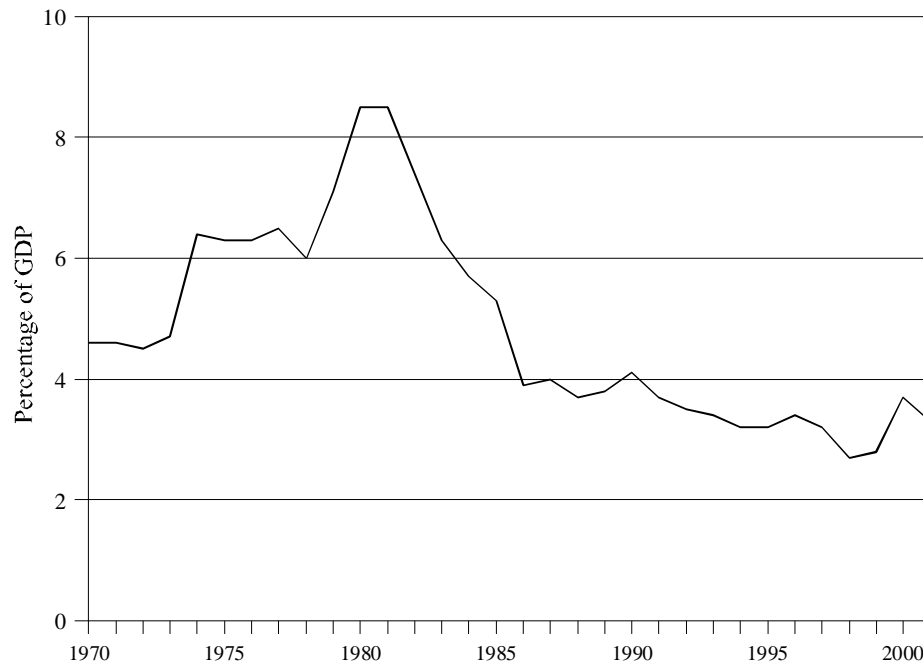
As **Figure 5** indicates, by the early 1990s the proportion of consumer expenditures on oil and gasoline had declined from the high levels of the 1970s and early 1980s. Data are not yet available to indicate what effect the price run-up starting in 2004 has had on this measure. Perhaps most important, the common view during the earlier crises was that oil prices not only were high, but were destined to become ever higher in the coming years. This view is no longer prevalent, and the general expectation has been that the price increase is a temporary phenomenon, although lasting longer than expected. The current crisis has led to some analytical speculation that world oil production has peaked, but additions to proved world oil reserves seem to contradict that thesis. Most oil industry analysts appear confident of a long life remaining for the resource and argue that if oil is replaced, it will be because of improved alternative technologies, not because the world is running out of oil.

**Figure 4. Nominal and Real Price of Gasoline, 1973-2005 and April 2006**



**Source:** EIA, *Monthly Energy Review*, May 2006, Tables 1.6 and 9.4, calculated by CRS.

**Figure 5. Consumer Spending on Oil as % of GDP, 1970-2001**



**Sources:** Calculated by CRS with data from EIA, *Annual Energy Review* 2005, Table 3.5. GDP from Bureau of Economic Analysis, Department of Commerce.



## Policy Options

The several energy crises of the past led to major legislative action, twice in the 1970s and once following the 1991 Gulf War. The Energy Policy Act of 2005 differs from the previous actions because Congress had been considering major energy legislation for three years before the situation became a nationwide concern. By the time the bill finally moved through Congress, the major issues had already been fully debated and the final version differed little from previous initiatives, except for resolving a number of issues that had blocked passage before.

As in previous legislative energy debates, a major policy divide existed between those who view the gasoline-fueled automobile as a temporary necessity to be tolerated only until a substitute fuel or alternative means of transportation can be developed, and those who expect oil to be the same dominant transportation fuel in the indefinite future that it is at present. Compromise agreements have been reached via a combination of measures that enhance the development of alternatives or restrain the growth in demand for oil, on the one hand, and those that increase production or reduce the cost of supplying that demand, on the other, and this process led to passage of the comprehensive Energy Policy Act of 2005.

However, as gasoline prices continued to surge, and damage to Gulf of Mexico oil and gas resources and facilities by Hurricane Katrina was assessed, calls for further measures to address the crisis were heard, although the 109<sup>th</sup> Congress adjourned after passing only one bill, lifting some restrictions on oil and gas leasing in the Gulf of Mexico. Continued price pressure, and the change in leadership in the 110<sup>th</sup> Congress, has already stimulated further legislative initiatives.

The following section describes legislation taken up during the second session of the 109<sup>th</sup> Congress, as well as proposals being considered currently.

## Oil-Related Legislation

**Reducing Impacts on Consumers.** A number of proposals are aimed at easing the impact of high prices on consumers, or are aimed at the oil industry's price-making policies.

**Price Gouging.** The rapid increase in gasoline prices following the Katrina disaster led to allegations of price gouging. P.L. 109-58 included a provision requiring the Federal Trade Commission (FTC) to conduct an investigation into price gouging in the recent increases in gasoline prices. H.R. 3893, as passed the House October 7, 2005, included provisions requiring FTC to define price gouging and penalize violators.

After gasoline prices surged again in April 2006, momentum increased for various price-gouging proposals. Several initiatives that would impose windfall profits taxes on crude oil profits were also introduced. On May 3, the House passed the Federal Energy Price Protection Act, H.R. 5253, by a vote of 389-34. The bill would require the FTC within six months after passage to issue rules defining price

gouging in crude oil, gasoline, diesel, home heating oil, and biofuel, and would prohibit gouging so defined.

**Tax Relief.** On April 26, 2006, Senator Domenici proposed an amendment to the FY2006 emergency supplemental appropriations bill (H.R. 4939) that included a \$100 “Fuel Tax Holiday Rebate.” The proposal was cosponsored by Majority Leader Frist and other Senators. The amendment also contained provisions about price-gouging, easing restrictions on rebates for hybrid vehicles, and approving leasing of the Arctic National Wildlife Refuge (ANWR). However, the amendment was withdrawn May 2.

**Suspending Import Duties on Ethanol.** Because the latest gasoline price run-up was attributed in part to the need to increase use of ethanol, some Members, including Senate Foreign Relations Committee Chairman Lugar and House Energy and Commerce Chairman Barton, proposed suspending temporarily duties on imported ethanol, particularly from Brazil. President Bush also made a similar proposal. The action was strongly opposed by ethanol producers and their supporters.

**“Boutique” Fuels.** The Energy Policy Act of 2005 had some provisions related to local requirements for specific blends of gasoline, but some proposed legislation is aimed at further reducing “boutique fuels” requirements that, according to some observers, make the national gasoline market less flexible. H.R. 3893, the Gasoline for America’s Security Act of 2005, passed by the House October 7, 2005, by a vote of 212-210, would among other provisions require the Environmental Protection Agency to develop a Federal Fuels List and to limit local gasoline blends to those on the list. (For details, see CRS Report RL31361, *“Boutique Fuels” and Reformulated Gasoline: Harmonization of Fuel Standards*, by Brent D. Yacobucci.) Other boutique fuels legislation has also been proposed.

**Windfall Profits Tax.** Several bills introduced would impose taxes on oil companies in light of record profits recorded as a result of the crude and gasoline price run-up. The context of the proposals lies in the Crude Oil Windfall Profit Tax Act (P.L. 96-223) of 1980, as part of a compromise between the Carter Administration and Congress over the decontrol of crude oil prices. (For details, see CRS Report RL33305, *The Crude Oil Windfall Profit Tax of the 1980s: Implications for Current Energy Policy*, by Salvatore Lazzari.)

**Mid- to Long-Term Supply and Demand.** Most proposals affecting supply and demand of crude oil and gasoline would not affect the current short-term crisis but would be aimed at longer term trends.

**Fuel Economy.** Corporate average fuel economy (CAFE) standards also have a long history of controversy, going back to their establishment in the 1970s. In the mid-1990s, the National Highway Traffic Safety Administration (NHTSA) was considering a rulemaking that would result in increased standards for light-duty trucks (including sport utility vehicles), but for several years, Congress included in its annual appropriation for NHTSA a measure prohibiting NHTSA from analyzing or undertaking such a ruling. That prohibition was dropped in the FY2004 NHTSA appropriations, and a final rule issued by NHTSA in April 2003 requires a boost in

light-truck fuel economy to 22.2 miles per gallon by model year 2007. In the summer of 2005, the Bush Administration proposed new fuel economy standards for light trucks, to take effect in the 2008 model year.

During House floor debate on P.L. 109-58, an amendment to increase fuel economy standards to 33 miles per gallon over 10 years was defeated by a vote of 177-254. A more general amendment to the House bill, requiring the Administration to take “voluntary, regulatory, and other actions” to reduce oil demand in the United States by 1 million barrels per day from projected levels by 2013 was defeated 166-262. The measure was included in the bill passed by the Senate but was dropped in conference.

Continued high gasoline prices have raised congressional interest in higher mandated CAFE standards again. On January 22, a bipartisan group of 10 Senators introduced S. 357, the Ten-in-Ten Fuel Economy Act, which would raise standards for SUVs and passenger cars to 35 mpg by 2019. The President argues that standards should be set by the executive branch, not by Congress, and in his State of the Union speech on January 23, he set a goal of reducing gasoline consumption by 5% by 2017 through more stringent standards. The White House said that would be the equivalent of increasing CAFE standards 4% per year starting with model year 2010.

**ANWR.** Oil and gas exploration and development of part of the Arctic National Wildlife Refuge (ANWR) have been controversial for many years. This was part of the early proposals for legislation that eventually became the Energy Policy Act of 1992, but was dropped in the face of strong opposition in both houses. Support for action grew gradually through the decade, along with technological developments that advocates claimed would reduce the environmental impact of development. Numerous attempts to open the region for leasing were made, and both the House and the Senate at various times approved measures that included leasing provisions, but none of them survived to become law during the 109<sup>th</sup> Congress.

**Savings Goals.** A number of legislative proposals would have set goals for reducing oil consumption. An example is the Enhanced Energy Security Act of 2006 (S. 2747), introduced by Senator Bingaman May 4, 2006, which would have required the Director of the Office of Management and Budget to develop an action plan to save 2.5 million barrels per day (mbd) in 2016, 7 mbd in 2026, and 10 mbd in 2031.

President Bush took up the idea in his State of the Union speech on January 23, 2007, calling for a cut in gasoline consumption of 20% in 10 years, through a combination of increased fuel economy standards (see above) and increased mandated use of alternative fuels (see below).

**OCS Leasing.** The moratorium on oil and gas leasing in the Outer Continental Shelf (OCS), except in the central and western Gulf of Mexico and some parts of Alaska, was subject to much controversy during consideration of P.L. 109-58. A proposal to allow states to voluntarily opt out of the moratorium was dropped under threat of filibuster, and a measure to order the Department of the Interior to perform an inventory of OCS resources barely survived the debate.

Following the disruption of production by Katrina, momentum to lift the moratorium increased, and some supporters suggested it might be included in the budget reconciliation process. The House Resources Committee on September 28, 2005, marked up a bill that would have given states the option of allowing drilling for petroleum and natural gas. In approving the bill, the committee adopted an amendment that would lift the moratoria on drilling the OCS for natural gas completely. In the face of opposition to the natural gas provision, Representative Pombo, Chairman of the Resources Committee, decided not to bring the bill to the floor as planned.

On October 26, the Resources Committee, as part of its package of measures for the budget reconciliation bill, included provisions that would make statutory the current presidential moratorium on OCS leasing until 2012 but would allow individual states to opt out of the moratorium and would allow states close to 50% of the royalties from oil and gas production that resulted. It would also give states the option to extend the moratorium after 2012. However, the provision was removed from the bill (H.R. 4241) before it was passed on November 18 by a vote of 217-215.

On May 10, 2006, the House Appropriations Subcommittee on Interior and the Environment voted to lift the congressional suspension of natural gas leasing for much of the OCS. The legislation, if approved, would leave in place the presidential moratorium on the same region, which operates until 2012.

On June 29, the House passed H.R. 4761, the Domestic Energy Production through Offshore Exploration and Equitable Treatment of State Holdings Act of 2006, which would lift some of the restrictions on OCS leasing. On August 1, the Senate passed S. 3711, the Gulf of Mexico Energy Security Act of 2006, which would lift some restrictions in Gulf of Mexico oil and gas leases. This provision was included in H.R. 6111 (P.L. 109-432), the Tax Relief and Health Care Act of 2006, which passed the House on December 8 and the Senate the following day. (For details, see CRS Report RL33493, *Outer Continental Shelf: Debate Over Oil and Gas Leasing and Revenue Sharing*, by Marc Humphries.)

**Refinery Revitalization.** P.L. 109-58 contained some provisions to encourage construction of new oil refineries, but the damage to refining facilities caused by Katrina in the Gulf of Mexico area led to calls for further measures. On September 28, 2005, the House Energy and Commerce Committee reported out H.R. 3893, the Gasoline for America's Security Act of 2005, and the House passed the bill October 7 by a vote of 212-210. Among other measures, the bill would provide for presidential designation of potential refinery sites on federal lands and military bases that are closing, and would set up a process for coordinating authorization and related environmental reviews for construction of new refineries, to be led by the Department of Energy. It would centralize judicial review of the process in the U.S. Court of Appeals for the District of Columbia. The bill, as reported, would also have amended the Clean Air Act regarding provisions for New Source Review for refineries and other facilities, but the measure was dropped before being brought to the House floor. (For details, see CRS Report RS21608, *Clean Air and New Source Review: Defining Routine Maintenance*, by Larry Parker.) The bill also contains measures concerning boutique fuels (see above).

A similar bill was introduced in the Senate September 26, as the Gas Petroleum Refiner Improvement and Community Empowerment Act, S. 1772, but the bill was rejected October 26 by the Environment and Public Works Committee by a vote of 9-9.

On June 7, 2006, the House passed the Refinery Permit Process Schedule Act (H.R. 5254), by a vote of 238-179. The bill would require the President to appoint a “federal coordinator” to organize the permitting of new refineries.

***Presidential Proposals: Alternative Fuels.*** In his January 31, 2006, State of the Union message, President Bush set the goal of breaking the U.S. “addiction to foreign oil” and of “replacing” more than 75% of oil imports from the Middle East by 2025. The main thrust of the presidential initiative was to increase funding for research in producing ethanol from plant fiber biomass (rather than from corn), for improved batteries for hybrid automobiles, and for hydrogen fuels.

In his most recent State of the Union speech, on January 23, 2007, the President went further, setting a goal of reducing gasoline consumption by 20% in 10 years, through a combination of more stringent fuel economy standards and setting a mandatory renewable fuels standards of 35 billion gallons of renewable and alternate fuels by 2017, about five times the current consumption. The current target, set in the Energy Policy Act of 2005 (P.L. 109-58), is 7.5 billion gallons by 2012.

## Legislation

### **H.R. 6 (Rahall)**

Creating Long-Term Energy Alternatives for the Nation (CLEAN Energy) Act of 2007. Passed by the House January 18, 2007.

### **S. 357 (Feinstein)**

Ten-in-Ten Fuel Economy Act of 2007. Introduced January 22, 2007.

## For Additional Reading

### CRS Reports

CRS Report RL33523, *Arctic National Wildlife Refuge (ANWR): Controversies for the 109<sup>th</sup> Congress*, by M. Lynne Corn, Bernard A. Gelb, and Pamela Baldwin.

CRS Report RL31361, *“Boutique Fuels” and Reformulated Gasoline: Harmonization of Fuel Standards*, by Brent D. Yacobucci.

CRS Report RS22236, *Price Increases in the Aftermath of Hurricane Katrina: Authority to Limit “Price Gouging,”* by Angie A. Welborn and Aaron M. Flynn.

CRS Report RL33290, *Fuel Ethanol: Background and Public Policy Issues*, by Brent D. Yacobucci

CRS Report RL33413, *Automobile and Light Truck Fuel Economy: The CAFE Standards*, by Brent D. Yacobucci and Robert Bamberger.