Senate Democratic Policy Committee Hearing

"An Oversight Hearing on Record High Gasoline Prices and Windfall Oil Company Profits"

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Transcript

DORGAN:

We will call the hearing to order today. This is a hearing of the Democratic Policy Committee. My name is Senator Byron Dorgan. I'm joined by a couple of my colleagues. We will be joined by others. I'm joined by the Democratic leader Senator Reid and also Senator Jeffords. We are here today to talk about the issue of oil and gas prices in this country.

I want to give just a brief summary to begin this hearing and talk a little about why this is such a significant issue. Obviously the most important issue here is the price – the price at which we receive our energy. Let me give a couple of numbers if I might.

In this world at this point, we use about 84 million barrels of oil a day. 84 million barrels of oil a day. We in the United States are five percent of the world's population and we use one-fourth of that: we use about 21 million barrels of oil per day.

(Audio disappears)

…February 1st of last year 2004, the price of oil, a barrel of oil, in this country was 34 and a half dollars a barrel – about 35 dollars a barrel. In all of the year 2004, the average price of a barrel of oil was 40 dollars a barrel. Now, since that time, the price of a barrel of oil has increased dramatically. I would say to you that at 40 dollars a barrel, the oil companies had the largest profits in their history.

Since that time, the price of a barrel of oil has gone 25 and 30 dollars a barrel above that – above the point at which the oil companies experienced the largest profit in their history. I believe those are windfall profits or excess profits. Those profits come to those oil companies as a gain to them, but at great expense and great pain to those people in this country who must purchase gasoline that is derived from that oil. So the question is: is it fair in this country to see the oil industry profit far above anything they have ever experienced, far above the experience of any other corporation as a matter of fact, at a time when consumers are hit with such extraordinary prices.

Now I'm going to show – we went to the internet and set up a site and I thought it would be interesting to show you 40% of the oil coming from this country, add 30 dollars a barrel to it, and you get 7 billion dollars a month, or 80 billion dollars a year in extra windfall excess profits. That's $2430 a second that goes into the oil company profits and this will run throughout the hearing and you will just get a sense of what it means to have nearly 2500 dollars a second in excess or windfall profits.

We did invite for this hearing to talk about these issues the chief executive officers of Exxon-Mobil, Conoco-Phillips, and Shell Oil Company. It's interesting to note that when I say Exxon-Mobil, I'd be talking about two companies some years ago, Exxon and Mobil, but through mergers and acquisitions, the oil industry has become much more consolidated, the companies have become much larger and much more powerful. Conoco-Phillips, I would have been talking about two different companies, but now it's one company. Exxon-Mobil, Conoco-Phillips, and Shell, through mergers, we have now a much more concentrated, a much more powerful industry.

I don't object personally, speaking for myself, I don't object to profits in the oil industry that are sunk into the ground to explore for more energy. I believe that is worthy and something to be done, and yet I read in the newspapers that Exxon, for example, Exxon-Mobil, is busy buying back their stock. So you amass excess or windfall profits and use a portion of it to buy back your stock. That in my judgment is unjustifiable. And I think most consumers in this country would understand and would agree that these excess profits that currently exist are at great pain to American consumers.

Now I want to make a couple final points. One, this issue of the excess or windfall profits existed prior to Hurricane Katrina. It is true that Hurricane Katrina has proven some further dislocations and further advanced the price. That's come down a bit off the high at this point. But this issue existed in August before Hurricane Katrina hit. We have to ask tough questions in this country about the price of energy, the access to energy, and who gains and who pains.

The answer today is very simple. The major oil companies in this country, with respect to the 40% of the oil that they produce for this country, aside from the record profits they showed last year at $40 a barrel, are now experiencing the windfall or excess profits that are above and beyond anything anybody ever would have expected in this country.

But it comes at a cost. And the cost is the farmers that are trying to fuel up their combine and harvest their crop. The cost is the drivers that drive up to the gas pump. My neighbor with a car of 15 gallons and his son's car of 15 gallons got 30 gallons of gas and paid $103 not long ago at the gas pumps. And the American people, whether it is gassing up their car, or facing a 70% increase in natural gas prices this fall as we go into the home heating fuel season, particularly in northern regions like Minnesota and North Dakota and other areas.

The question has to be asked by the Congress: "How is this justified; what's happening; what's causing it; and what can we do about it?"

The final point I would make is this: I have introduced one idea which is a windfall or excess profits recapture that would recapture part of those profits and use them to rebate to the consumers. These profits are unjustified at these levels and they ought to be recaptured and rebated to consumers. I would exempt from that that which is used completely for exploring for new energy.

This cannot continue to go on. It will have substantial dislocation for our country, for our people, and I worry in addition to all the things I just described, I also worry about this country's economy and whether this will be just a hiccup or whether this could throw this country into a recession in the long-term because the price of energy flows through virtually everything that is done in this country.

We have to keep our eye on the ball. We have to stare truth directly in the eye. And the truth is this energy problem is a serious problem that's causing a lot of pain and could cause havoc for this country's economy and Congress needs to do something about it.

Having said that, let me call on my colleague from Nevada, the Democratic leader, Senator Reid.

REID:

Mr. Chairman, I'm wondering is Mr. Raymond, Mr. Mulvin, Mr. Hofmeister going to take their chairs?

DORGAN:

Senator Reid, we did invite all three to be present. We wanted to have a discussion about these policies with three CEO's of energy companies. All three companies indicated to us that they would not be able to attend today, would not be attending this hearing.

REID:

Certainly not because they couldn't afford to come? It's expected that profits of these three oil companies this year, net profits will exceed $100 billion, so I think that they certainly could have arranged with their company planes to have gotten here.

Mr. Chairman, I'm grateful to you for arranging this meeting. This is a desperate move, I'm sorry to say, because committees here controlled by the White House, in this

Congress, refuse to do oversight. Refuse. We're doing it under the auspices of the Democratic Policy Committee. And I appreciate very much your arranging this hearing. The witnesses you have are just outstanding. I apologize. The Senate comes in at 2pm and I have to be there with Senator Frist.

But I've read the testimony that these witnesses are going to give. I looked particularly at Patrick Meadowcroft, who runs a service station. My brother ran a service station for many years – he's deceased now – he died as young man – but in going through his testimony, it reminded me of my brother. People used to think that the gas he sold, he made a lot of money.

Then and now, service station operators don't make much money on the gas they sell. What they try to do is to get gas as at a decent price and they're told how much they can mark it up. It's always just a little bit. They make their money on tires, batteries, accessories, and now hot dogs and cracker jacks and stuff you can buy in the little stores they have. He outlines very clearly how he's concerned that he's not going to have a business to pass on to his children.

America can do better here than what we have here. From Nevada, to North Dakota, to Vermont, to Minnesota, people are paying too much for gasoline. That's an understatement. And this administration has no plans, no oversight, and there's no action.

I repeat, America can do better. Democrats believe we can change our future and make America energy-independent. Energy independent. We just finished an energy bill—Conoco-Phillips, Exxon-Mobil, Shell Oil— they did great with that bill. The American public didn't do so well. We didn't do anything to lessen our dependence on foreign oil. Nothing.

We have made some little gestures to try to say we're going to reduce our importation of oil. Now remember, Senator Dorgan said we used 21 or 22 million barrels a day. We said, "let's in the next few years, reduce our importation of oil by a million barrels." On a party line vote that was turned down. We lost that, if you can imagine that. We lost that vote.

In the wake of Katrina, things are worse. Gas prices we know shot up. In my neighborhood here, one of the marquees only had gas at $3.79 a gallon. Las Vegas is much like Reno, and certainly they're both like California – highest gas prices in the country.

Senator Dorgan mentioned two people pulling in filling up their cars, 15 gallons each. People have bought, right or wrong, they bought these big pick-ups, SUVs, and other things, that suck up the gas. I talk to my friend who has a pick-up truck and he filled up his gas tank – over $100. Now admittedly, he has a large gas tank, but one vehicle.

So I am terribly concerned that we are not doing our job here. To do our oversight, what is that all about? It's having Congress take a look at what's going on in our society to see if we can do better. That's what this hearing's all about. We can do better.

$100 billion. These three companies? That's too much money. That's obscene. And there bringing in these big bucks and a guy like Patrick Meadowcroft is barely support his family. Now that's the truth. And he's only one example. Farmers, and others that you will hear from today.

So Senator Dorgan, thank you very much for arranging this hearing and doing the wonderful job you are as the chair of the Democratic Policy Committee.

DORGAN:

Senator Reid, thank you very much. Senator Jeffords?

JEFFORDS:

Thank you Mr. Chairman. I want to thank Senator Dorgan and other members of the Democratic Policy Committee for holding this important hearing today.

I am here today because gasoline prices are hurting Vermonters and consumers across the country. Vermont is as far north as you can go, and it's mighty cold. Vermonters are asking why price signals aren't bringing in new investment into the oil and gas industry to increase the supply of the refined product. They are tired of the same justifications for wild price fluctuations that follow predictable events, such as annual hurricane seasons, summer driving, and inevitable machinery breakdowns that come from running our national refineries at full capacity.

There's no doubt that the cost of more than $3 dollars a gallon for gasoline has raided the pocketbooks of Vermont families. These prices are truly a hardship, increasing commuting costs and hurting business. As concerned as Vermonters are about gasoline prices, they're even more concerned and troubled by a report about home heating oil cost projections for the winter.

While $3 a gallon gasoline is a family budget breaker, $3 a gallon heating oil is a life or death matter. According to the Energy Information Administration, a bigger proportion of homes in New England use oil for heat than in any other region of the country. The number of New England homes using oil ranges from 70% in Maine, to 59% in Vermont, and 39% in Massachusetts. High heating prices are causing families to switch to less costly but sometimes more polluting alternatives such as coal or wood. We heated wood in my house.

Instead of letting prices dictate what people burn to keep warm this winter, we should have a national goal to encourage cleaner, more efficient, and more price-stable sources of energy. I'm here today to hear more about the causes of these prices so we can adopt appropriate remedies and solutions. Right now, we are conducting an uncontrolled experiment with our constituents' pocketbooks. It is time for us to grab the reins back and conduct the necessary oversight over these energy markets. Our constituents deserve nothing less and that's why we're here today.

DORGAN:

Senator Jeffords thank you very much. Senator Dayton from Minnesota.

DAYTON:

Thank you Mr. Chairman, and I also want to thank you for holding this important hearing. I see that our first panel looks very much like the oversight hearings that we have not had in the Armed Services Committee in the last few months on the situation in Iraq. It looks like the hearings that we have not had in the Committee on Homeland Security and Government Affairs that I've requested on the failure of response by FEMA and other federal authorities to the catastrophe for Hurricane Katrina.

Once again I commend you, Mr. Chairman, for holding this hearing like the one last Friday on the irregularities related to the Army Corps of Engineers and their contracting procedures. I read over the weekend, once again, further investigative stories about the profiteering going on by the private sector, those that were unfortunately taking advantage of the misery, the horror that is going on there.

These hearings, thanks to you, are at least being held, but they should be held in the regular Senate committees as you and Senator Reid, Senator Jeffords have also pointed out. This is just atrocious. It is irresponsible and it's indefensible that we cannot get responsible authorities who appear before duly constituted Senate committees, and when we cannot get the duly constituted Senate committees, controlled by the Republican leadership and really, controlled also by the White House, to bring responsible, or in this case, irresponsible officials before the American people. Not just before us as Senators, but more importantly, through televised hearings before the entire American people so they can get answers as to why their prices are going up.

And you just said Senator Jeffords, in Vermont and Minnesota, like North Dakota, Minnesotans have been gouged at the gasoline pump for prices, as you said Mr. Chairman, were already going up from a 3 month period before Hurricane Katrina hit, by about 60 cents nationwide and three days, just three days after Hurricane Katrina struck, the gasoline price in Minnesota went up an average of another 45 cents.

In a two week period including Hurricane Katrina's aftermath, the price of gasoline in parts of Northern Minnesota went up by almost a dollar. And we get all of our gasoline, all of our oil, in Minnesota, from Canada. We don't have any supplies coming from the southern United States. This was not due supply disruption. It was due to those who are taking unfair advantage of the situation and gouging Minnesotans at the pump.

Now President Bush said in the immediate aftermath of Hurricane Katrina, this is a quote, "there ought to be zero tolerance of people breaking the law during an emergency such as this, whether it be looting, or price gouging at the gasoline pump, or taking advantage of charitable giving or insurance fraud."

But actions speak louder the words Mr. Chairman. Unfortunately, I don't see any signs so far that the administration tends to do anything, either through executive branch action or prosecution by the Attorney General by legislation being proposed. That's why I proposed legislation, you described yours, I proposed legislation that has been introduced that would go after this price gouging matter and give the Attorney General the authority, and I hope he would actually use it, to investigate and then to prosecute these instances of price gouging.

This is legalized stealing. This is immoral and should be illegal and unfortunately right now under federal law it is not.

Lastly I just point out Mr Chairman, echo what you said about the profiteering, an article that appeared a week ago in the *Wall Street Journal* and it says, "After Katrina, Refiner Shares Hit New Gear." Not two weeks ago shares for the nation's refineries looked poised for a breather, after a long and profitable run. Then came Hurricane Katrina. As a result," skipping ahead, "shares of San Antonio-based Valero Energy Corporation, the nation's largest refiner have jumped 25% from before the storm. U.S. refiners have averaged a 24% gain in share price since the market closed on August 26th, the Friday before Katrina blew ashore, and a 129% gain in the value of their shares for the year to date. By comparison, the banks' oil exploration and production index is up 6 and a half percent since the storm and 36.9% so far this year, while the overall stock market is only modestly in the black for the same periods."

Once again the market is showing the expectations of the kind of profiteering that you have described Mr. Chairman. I salute you for the legislation you have introduced. I strongly support it and I would urge that the Republican leadership in the Senate, on behalf of the American people, step forward and do something about this outrageous profiteering and price gouging. Thank you.

DORGAN

Senator Dayton, thank you very much. Senator Feinstein of California.

FEINSTEIN

Thank you very much Mr. Chairman. The price of gasoline in my state, which is a very large state, the largest state, is about 3 dollars a gallon, about $2.79 I gather in other states. The Energy Committee did have a hearing about this. I thought it was an unsatisfactory hearing.

I pointed it out at that time, Mr. Chairman, how the oil companies have really experienced unprecedented profits. The projections for the rest of the fiscal year, based on second quarter earnings and second quarter earnings, are unprecedented in their amounts.

Although I realize that there are different profit centers in different oil companies, it seems to me that there should be voluntary price restraint in this industry. I wrote a letter to each of the CEOs of the oil companies that serve California, big companies, and asked them to consider voluntary price restraint for the reason that Californians have long commutes. It's not uncommon for the working person to buy three tanks of gas a week. So the difference in price is enormous and a real impact of the lifestyle of Californians.

Well, I got letters back. I must say that they were really unresponsive. There was a lot of material in them and would like to make them available if I might for this record.

I also had occasion to meet with Sir John Brown at a social event somewhere else and he of course is CEO of BP, which owns ARCO, and has the lowest gasoline prices in California, and I do appreciate the fact that they have been able to keep gasoline prices somewhat down.

But just to give an idea of the profits, Exxon Mobil's first half profits translated into annual profits of 31 billion dollars. That's more than the $25 billion in 2004 and far more than the $15 billion of 2001. ConocoPhillips first half profits translate to annual profits of $12.12 billion, that's up from the $8 billion in 2004. BP, again, in 2005, translate to annual profits to 20.9 billion dollars, as compared to $16.9 billion, in '04. And Shell's first half profits for '05 translate into annual profits of $20.3 billion as compared to $17.2 billion.

So there is no question in my mind that big oil is making big profit on the backs of the American worker who has to use gasoline to get to and from work. And I have a hard time understanding why they will not engage in voluntary price restraints. I think until the Congress really shows the muscle to take action that what we are going to see is pretty much the response that I got to my letter, which is kind of a fluff off.

As you all know when we passed the Commodities Modernization Act of 2000, the one area, energy and metals were left out of anti-fraud manipulation and oversight by the CFTC. The only exemption from this kind of oversight is really in the energy sector.

As someone who went through the electricity crisis in California, when one year, the total cost of energy in my state was $7 billion, and the next year it was $28 billion, there's no way that supply & demand can produce those kinds of numbers, and it has really led me to believe that the energy sector, by and large, is really, a very unusual sector of our economy because they, I think, have been allowed a wide margin for just taking any profit they possibly can wherever and however they can take that profit.

I think we as Democrats have to speak up, and have to begin to say "that day is over." Energy isn't "post-hosties." People live or die based on energy, and I think the entire industry needs a great deal more oversight, and in this area, we ought to take some action to retard price hikes in an emergency situation. Thank you very much.

DORGAN:

Senator Feinstein, thank you very much. Let me just make a point, given these comments. I don't think there is a free market in oil, though I know there will be those who say it is a robust, vibrant marketplace. I think that's nonsense.

In oil, what you have are some OPEC country oil ministers sitting around a table, talking about their notions of price and supply; then you have larger and larger oil companies, that have grown larger through mergers, that have more control of the marketplace, and more economic clout and power; and third, you have a futures market that is supposed to provide for liquidity, but in fact goes well beyond the provision for liquidity with now, rampant speculation in the futures market.

So you have all three things, which, in my judgment, clog the marketplace of free enterprise. They clog the marketplace of the free market. I think the result is a run-up in prices that is wholly unjustified. My colleague from California describes a circumstance with respect to wholesale electric rates in California, and it's an apt metaphor, because at that point, no one was interested in looking over the shoulders of those people who were, at that point, controlling supplies and manipulating price.

Government must have the capability to be a referee with respect to a market system when the market system no longer works, or at least, does not work for everyone. And so I appreciate very much the comments of my three colleagues.

I do want to mention one additional point. Someone made the point after one of our previous hearings that these were not duly constituted hearings. In fact, this is not an authorizing committee, but the Democratic Policy Committee was created, by law, in 1947, along with the Republican Policy Committee, and the law clearly implies the capability of holding hearings, talks about witnesses and other things.

We hold hearings in the Democratic Policy Committee. We have a standing open invitation to Republicans to join us at any and every one of our hearings. They have not wanted to do that, but we continue to have an open invitation to them.

This issue of the gas price, the oil price, is not about Republicans or Democrats. It's about whether the American consumer is getting a fair deal, and the answer is "no." The major oil companies are seeing profits that are extraordinary windfall excessive profits, and the pain at the gas pump, and the pain on the farm, and the pain around this country by consumers is extraordinary, and they deserve to have someone do something about it. That's the purpose of this…

FEINSTEIN:

Mr. Chairman, would you allow me one other comment.

DORGAN:

Yes, of course.

FEINSTEIN:

I forgot to mention this, and I hope the people from the oil community that's going to speak to us will mention this, and that is the closing of refineries. The fact that in the last decade or so some 30 refineries have been closed, because it's really more cost-effective for the community to run refineries at close to, or at capacity, and therefore, we can't really use the argument "well we have a shortage of oil supply." In my state, even if you had more supply, it couldn't be refined, and I think that's something that we ought to take a look at.

DORGAN:

Good point. I mentioned before you came, Senator Feinstein, that we had invited the CEO of Exxon-Mobil, the CEO of Conoco-Phillips, and the CEO of Shell Oil, and they chose not to come today, and so we will not hear their thoughts, but we will have a standing invitation to them and their representatives, and we will convene a Policy Committee hearing at any moment they wish to be present and give us their analysis of the kind of things we just described.

We have five other witnesses and I'd like to begin calling them to the witness table. Mary McCaffrey lives on Spring Rain farm in East Taunton, Massachusetts. If Mary wants to come forward and take her chair at the table, we will put up a name plate. Mary McCaffrey is a farmer.

Trisha Young-Williams. She works for Montgomery county schools and health services. And Patrick Meadowcroft, the owner of Maryland Line Service Center, is a proprietor of a family-owned, independent gas station in Parkton, Maryland.

Following that, we will hear from Mark Cooper, who is with the Consumer Federation of America, the director of research. Dean Baker, an economist and co-director of the Center for Economic and Policy Research in Washington, DC.

But first, Mary McCaffrey, you are a cranberry farmer, I understand, from East Taunton, Massachusetts. Welcome to Washington, DC, and you may proceed.

McCAFFREY:

Thank you very much. Senator Dorgan, Senator Jeffords, Senator Dayton, and Senator Feinstein, thank you so much for inviting me to come to Washington today to make my presentation.

My husband Billy and I live on our 200 acre mixed use farm with our two teenage children William and Sarah. We live about an hour south of Boston. Of this 200 acres, we have approximately, 80 acres in woodlot, 30 acres in hayfields, 11 acres of cranberry bogs, and ½ acre of pick-your-own strawberries…

DORGAN:

Excuse me, what is a cranberry bog?

McCAFFREY:

You would have to ask.

DORGAN:

If it takes too long…

McCAFFREY:

A cranberry vine is a perennial plant so once they're planted, their basically in forever. We have many bogs that have been in there for decades upon decades, so as you'll see later, that leads to some other options that we don't have. Some places call them marshes. We call them bogs.

The balance of our acreage is new growth woods, wetlands, and ponds, which supply water for the farm operations. The farm we live on was once a dairy operation and my husband grew up working on his grandfather's farm nearby. But milking cows is not a viable option on a farm this small so we started planting bogs 21 years ago. We taught ourselves from scratch, attended meetings, and adapted to changing conditions of production and marketing.

In the tradition of many other family farms we all pitch in as much as possible, as well as having a part time employee. We need another income source, which is carpentry. We feel committed and connected to our land because not only do we work here, we live here. We plan and hope to be able to hand our farm to the next generation.

On August 28, I filled my car in Maine for the trip home after our family vacation. I looked at the gas pump that said $2.65 per gallon mid-grade price and thought "Well soon I'll be home in Massachusetts and be paying far less than that." Little did I know that 96 hours later I would have to wait in line to pay $3.25 per gallon and actually see some gas stations with no gas. All of a sudden, every mile we drive was questioned and a tinge of panic was in the air.

What did we do to respond to this sudden change? For business, I can consolidate my trips to the lumber yard, bank, or agricultural supply house. On a personal level, I no longer make two trips to pick up our kids at separate schools for clubs and sports practices. They must wait now for a significant amount of time – I should have added "hopefully" – doing homework in the meantime, and wait for my one daily trip to town.

How can we reduce the fuel used by our hay equipment, tractors, trucks and chainsaws? This fall we are considering not cutting our third crop of hay at all. Fuel costs are up twenty three percent. Our bone dry summer has reduced yield to the point that it might not make economic sense to even cut it. Raising cranberries gives us no choices, however. We cannot let the bogs lie fallow or rotate crops. The bogs must be flooded for fall harvest and reflooded to be protected from winter's freezing weeks. If there is not sufficient rainfall, as there wasn't this summer, the pump supplies water through the irrigation system, which is a series of pipes buried underground beneath the plants – it's permanently there. This summer's heat and drought forced us to irrigate almost every day instead of every fourth or fifth day.

The other crucial use of the irrigation system is to protect spring flowers and fall fruit from freezing. There is motion of the water that is being sprayed by the irrigation system, and warmth generated by the heat of fusion, which occurs at 32 degrees, and protects the fruit and flowers from internal injury. During an average fall we will be running the pump for frost protection about 15 nights until picking ends in November. Mother Nature is the one who decides how much fuel we use.

Another aspect of the cranberry business is that we are not paid upon delivery of our fruit. We pay for fuel today but we won't receive any money for at least a month and final payment is many months after that. The price itself is dictated by the handlers. We do no direct marketing of fruit because the vast majority of berries are processed and frozen and turned into juice for future use. So, in other words, we don't have stands, like I have pick-your-own strawberries, you don't come to our farm to buy cranberries – I might have a couple hundred pounds in the garage, but that doesn't go very far. So there is no way to pass on any cost increases to anyone but ourselves.

I mentioned earlier that we have a wood lot and we sell between 20 and 40 cords of wood a year and if I did what the oil companies did, I'd increase my price from last year's price of $185 a cord, and maybe I'd say, "Oh look, maybe I can make some extra money charging $240 a cord." But I couldn't look myself in the mirror and I certainly couldn't feel comfortable with myself if I did that to people.

I hope we learn some lessons from this sudden crisis. We shouldn't need any more reminders of how fragile our fuel system and economy really are. We must research alternative fuels and learn to conserve and efficiently use the energy we have.

Thank You.

DORGAN:

Mrs. McCaffrey thank you very much for being with us. We will hear all of the witnesses before we ask questions. Next is Trica Young-Williams. Trica is a hearing and vision technician for the Montgomery County school health services, mother of a five-year old daughter, an eight-year old son, and a member of the Montgomery Country community action board, where she works on behalf of low-income families. Mrs. Young-Williams thank you for being with us, you may proceed.

YOUNG-WILLIAMS:

Mr. Chairman and members of the Committee, my name is Trica Young-Williams. I live in Silver Spring, Maryland and have a great son and a great daughter. I work in the schools as a Hearing and Vision Technician. I am here today to explain to you the very real cost that higher gas prices impose on American families — families like mine.

As a schoolroom health aide, I am able to spend the summer with my eight-year-old son and five-year-old daughter. Because I am not working, however, the summer sometimes imposes an extra financial burden on our family; for those three months, we must rely solely on the income that my husband, Grant, makes as a maintenance worker.

With the high prices at the pump, gasoline has become an extra bill each month. It's something that I have to take into account each day as I care for my family. On the warmest days during the summer I may not take my children out in the car, because driving with the air conditioning will require more gas. When I do go out, I decide more carefully which routes to take, so that I can get where I need to go using as little gas as possible. At over $3.00 per gallon, it definitely makes a difference.

The price of gas has also affected other decisions that I make on a day-to-day basis. I used to drive to buy groceries at the Shoppers Food Warehouse, because the prices were slightly lower than the local Safeway. With the added price of getting there, however, I now go to the Safeway because it was costing too much gas to get there to the "Shoppers" and back home.

Most importantly, the added price of gas has affected how I care and provide for my children. This summer I had to choose activities more wisely when it came to taking my children out on what I call their "field trips," due to the high gas prices. I had to take into account what it would cost to take them somewhere, as well as the price for the activity once we reached our destination. For example, because I thought gas prices would come down – I seemed to be pretty optimistic at the beginning of summer – I planned to drive my children to camp in Olney, which is about 20 minutes away, for camp. Once the prices were still going higher, we decided we had to take the kids out of the camp because the drive became too expensive with the price of the camp as well. After that happened I had to be more creative in finding alternate activities that were free and stimulating to the children, like free concerts and trips to the local library. The higher gas prices had a very real effect for our family.

My story is centered around my children; because I don't work during the summer, during the summer, my children are my job. I can only imagine how it feels from when I talk to people and see how much they and myself pay at the gas pump, and how hard it is to worry about getting to your job daily so you can make money to support your family. Please keep that in mind as you work on this important issue.

Thank you.

DORGAN:

Mrs. Young-Williams, thank you very much for being here. And now we have Patrick Meadowcroft. Patrick is a proprietor of the Maryland Line Service Center, a family-owned independent gas station in Parkton, Maryland. He's worked in the gasoline service station industry since 1964, and has owned or operated both independent and branded gas stations. His current station, Maryland Line Service Center has remained independent for 34 years.

Mr. Meadowcroft, I should tell you that my father ran a gas station and so, as is the case with all sons of people who run gas stations, when you are tall enough to reach the gas tank, you start pumping gas. So at nights and on weekends, through most of my early life, I pumped gas. Some people say I have not changed vocations, but I know a little about gas stations, and I appreciate very your being here to give us your story today.

MEADOWCROFT:

Mr. Chairman and members of the Committee my name is Patrick Meadowcroft and I've been a citizen of this country all my life. I have been in the gasoline business since 1964. Over the years I have owned both independent and branded gas stations, including Gulf, Chevron, and Exxon stations. My current business, Maryland Line Service Center has been there for 24 years. The prices of the fuel we purchase, however, makes me fear that I may not have a business to pass on to my daughter, who's running my business, and my grandchildren.

My station's located a half-mile from Maryland's border with Pennsylvania, and I've always had trouble being close to the state line. Compared to Baltimore County, where my station is located, Pennsylvania has lower taxes on gasoline and fewer environmental regulations. Although I support our environment, and want clean air for my grandchildren, they do make it harder to compete when your station lies across the state line. The cleaner air in Maryland, we have to pay additional costs for our gas right there. Until recently, however, we were able to meet those obligations and compete as a successful, independent, family-owned business. With the rising price of gasoline, I don't know how long this will continue.

Before I go further, I'd like to clarify some common misunderstandings about how gasoline prices work. Everyone knows that prices at the pump have been going up, but not everyone understands that gas station owners don't set prices independently. We set our prices based on what we pay for the gas we sell. We make a very small margin on gas, and rely largely on other products that you buy at the gas station — everything from a can of oil to a cup of coffee. When you pay more to fill up your tank, it's because the station owner paid more to fill up his station's tank, so it's passed on to me.

Most recently, the effects of Katrina have been felt very deeply by all business owners. The effect on the fuel and transportation industry is worse than anything I can remember since the gas crisis of the 1970s. In the 1970s, the retailers were given fuel allotments at the same price. In 2005, as an independent station, our cost to *purchase* fuel is 20 to 40 cents more than the cost at which a branded competitor is *selling* its fuel. This puts me out of business. I recently purchased regular gas at $3.49 per gallon, which was the best price I could get from seven or eight suppliers, but had to sell it at $3.19 per gallon just to move my inventory, because in order for me to get a lower-priced gas, I had to get the gas out of my tank that I had in there. That means a 30 cent loss for every gallon I sold, just to get a lower-priced gas, where I had paid an exorbitant rate for the gas I already had in my station. Even though I was losing 19 cents a gallon, my customers complained to me about the high prices. My prices were still high even though I was losing money on it. My distributors literally suggested that we temporarily go out of the gas business. We have managed to keep it going, but our sales dropped from 2,500-3,000 gallons per day to as low as 550 gallons per day. You can imagine what an 80% decrease in business can cause – you're technically out of business.

We're struggling to keep our family business alive and lucrative for generations to come. At this rate, that's impossible. My daughter, Ayda, has managed the business for 13 years, and several years ago she had to start a second job – she went into real estate just to feed her own family because the business wouldn't sustain it.

Plus, it seemed to me that the idea of the oil industry, it seems to me, is that they really want to do away with the independent, smaller gas operations, because they wanted sheets that costs two or three million to make a station then they serve everything.

I hope that, by being here today, I can help explain the differences that smaller gas station owners face, and that you can make America work better for small business owner like us. I thank you for your time. I appreciate the opportunity. I'm not really a great talker or anything, but I really wanted to be here because I feel that we do make America: The little man – and I've been proud to be in the gas station business for 40 years. There was a place for me, but after 40 years, you come up against something like this after you spend 40 years in a business and you're put out of business in a very short period of time, and this is what happened. It's from exorbitant rates; gas is going right through the roof.

It has come down, but even today before I came down here I wanted to check on the prices. My last load of gas I purchased, it cost me $2.71 per gallon. The place half a mile up the road from me is selling it retail at $2.72 a gallon. And I always put a mark-up on my gas, so technically when these gentlemen told me I should go out of the gas business, I am out of the gas business. I thank you for your time.

DORGAN:

Mr. Meadowcroft thank you very much. I do have a couple of questions, but I'd like to recognize that Senator Pryor from Arkansas has joined us, Senator Pryor if you have any opening comments?

PRYOR:

Mr. Chairman, I would thank you. Thanks for having this today.

DORGAN:

Mr. Meadowcroft, thank you for taking the time to come here today. You indicated in your statement as well in the last comment you made "our cost to purchase fuel is 20 to 40 cents more than what your branded competitors are selling theirs for." I assume that the oil companies have become larger and more concentrated and more powerful, is there a serious problem with independents being squeezed out of this business? Is it the fact that your competitor is a branded competitor and therefore has a natural pricing advantage up through the wholesaler of an integrated major oil company? Is that what's happening?

MEADOWCROFT:

The problem is right here, is the idea that all my jobbers are branded. They're individuals that work for the branded companies and they dictate right now, the big oil companies were keeping their product for their stations. So that right there makes a limited number of gallons that are left over and they're allocating it. Even today, they're allocating it. They only give you so many loads that you can give to your independent service station operation, so technically, I'm at their mercy.

DORGAN:

But this is your wholesaler...

MEADOWCROFT:

My wholesaler.

DORGAN:

The jobber is your wholesaler, that's who you purchase from? You say that is a branded wholesaler? Is that part of the major integrated company? The major integrated oil companies control from pulling oil out of the ground to pumping it into the gas tank of your car, so you as an independent are buying from a wholesaler that is part of a branded company?

MEADOWCROFT:

It's part of a branded company and the only thing I can get is their excess.

DORGAN:

And you're saying they have two different pricing policies, one to serve their branded stations, and then a higher price, which is their excess, or however they term that commodity that they sell to their independent stations, at a higher price…?

MEADOWCROFT:

At this time when you have a tight market, and I don't want to say this happens all the time because it doesn't, but when you have a tight market like you have today, the price is always higher. See I only get their excess, and if they say they have no excess, then technically I'm out of business and they won't give it to me. But if they did it like they did in 1974 where I get the same gas at the same price as my competitor then I could be competitive. But they're willing to give me the gas, but at whatever rate they choose.

DORGAN:

That's a problem. That is not a competitive marketplace. That is choking or clogging the arteries of the marketplace when you do that.

Mrs. McCaffrey, I come from a state with a lot of family farms and we don't produce cranberries, and I'm not sure we'd recognize a cranberry, but we produce wheat and corn and barley and sugar beets and a whole range of commodities, and I understand especially when you talk about the fact that when farmers are heavy users of energy, whether it's to take off the third alfalfa crop, or to put in the crop, or to harvest the crop later, or to till the soil, there isn't anyplace they can pass that energy cost along, is there because on the back end of your farming operation is a marketplace that tells you what you're going to get for your commodity and it doesn't matter what you paid for energy?

McCAFFREY:

Right. We do sell our hay to the individual people who come to our barn, but there again, I'm not going to, all of a sudden, jack up the price of that because I see an opportunity to "steal a few extra dollars," if you will, so it is a different set of circumstances.

DORGAN:

And I really worry what this does to farmers – fertilizer costs, which have a heavy energy component. I really worry that there are a whole lot of family farmers across this country that just can't pay these prices. They just can't do it.

McCAFFREY:

Well I have an underlying feeling that family businesses in general, not just farms, but gas stations, grocery stores, drug stores, whatever it is, this is the crisis of the moment is the fuel supply. But underlying all this, I think, the social and economic health of the country necessitates that whatever it takes to keep family businesses around, it doesn’t have to be the farms, only we really need it. You can’t have everything running out of a great big central warehouse somewhere – I don’t know where. It’s just very necessary. And I’ve felt for a long time that national security is one thing, and energy supply is just as important to national security, as anything else you want to do. It’s scary and it’s quite a lot unnecessary in my view so I really appreciate this.

DORGAN:

Well, this marketplace, I think, is a perverted marketplace. I don’t think this is a free market, and I’ve sat here and I’ve watched the big energy companies get married up. They have this abundance of affection for each another, and pretty soon you read in the paper that they’re going to get hitched, and so two companies become one, and four companies become one and pretty soon, you have just a few companies left with massive market power. And that market power is used to be able to squeeze, and that is not the way the free market is supposed to work.

So those of us who took and taught economics and Adam Smith and the “invisible hand” everyone doing that which selfishly is in their interest will contribute to the interests of the whole, that doesn’t work when you have large concentrations of economic power that can pervert the market system and clog the arteries of the free market. Let me call on Sen. Dayton for questions.

DAYTON:

Senator, I think that the invisible hand has become the invisible club, as you say, they can bully people into submission economically. Ms. McCaffrey, I think the fact that your conscience won’t permit you to exploit your customers is the reason that you can be here today and the previous panel declined to appear. I salute you for that and I think that each of you have spoke eloquently for what literally millions of Minnesota farmers, parents and business owners would be saying today about being at the mercy economically of these unfortunately very merciless drivers of these prices. I wonder that if the three non-appearing panelists of the energy company executives had been here, remained here, were here now, what would each of you like to say to each of them or all them, or would like to ask them to do as a remedy.

McCAFFREY

I guess I would ask them to look me in the eye and say tell me on a personal basis how you feel comfortable doing what your doing because obviously as a business person I understand that you have to make money, you have stock holders, I don’t have stock holders in my family business, but I understand, yes, you have to make a profit. But just gouging and raking in all you possibly can is not doing business. That can’t be the only thing that you think of.

DAYTON:

Ms. Young-Williams

YOUNG-WILLIAMS:
I guess I would feel like I would need to try and look them in the face also and appeal to them that there are people, like myself, and this is just a mild story compared to some of my friends who are really having a hard time getting to work, where it is not an option to take the bus, because we drop our kids off to day care. I would just them to please rethink, is their profit or the money that they seem to be making, according to how much its hurting us, really it's a big pain.

DAYTON:

As a parent myself, my children being a little older than yours now, but I can empathize how hard it must be to tell, 8 years and 5 years old did you say, that they have to be pulled out of the summer camp experience.

YOUNG-WILLIAMS:

We felt really bad, but it came to the point, like I said. I've been off for summers before, but never have we planned on gas as being a bill. And to tell them, listen, and it wasn't really way, but they really know "hey this is kind of a cool day" and we all have the joke in mommy's van "this is a cool day, no air conditioning", but my husband would kind of laugh about it, but he knew I had to conserve because most of the gas would be poured into his tank, since we are able to have two cars because he had to go to work, to and from work everyday.

DAYTON:

Mr. Meadowcroft.

MEADOWCROFT:

I think the first thing I would ask them is to be true Americans because for us to get 60% of our oil supplies from overseas is not necessary, we have a lot of oil. I would also ask them to take their large profits and I'm a business man, so I'm not averse to them making a profit, and if they would use some of there profits to make alternative fuels, where could keep our money in our own country, which is where your corn comes in, and the American average worker would actually be put to work, and we could help the farmers. We could use these things and with this large profit they made they could make this happen if they stay with the idea that there are Americans first, they should be Americans first, because America is what made them great in the first place. We do have ingenuity, I love that we live in America and we have this free enterprise system and that Americans are ingenious, we are a lazy people that take our laziness, and make it a better way of doing things. I don't want to be a hard working laborer, I want to be one of them, I want to go forward. These gentleman here the opportunity here to make America better than it ever has been by taking their large profits and making alternative fuels or even giving us more fuel efficient cars, and doing what would make America great. We are our brothers' keeper, one for one and one for all. We have to look after each other. And we have proven it with Katrina down here, and let's carry it a step further and get out wealthy oil companies do the same thing to help us have a better America.

DAYTON:

I think it was Mahatma Gandhi who said "there is enough in the world for human need, there is not enough for human greed", and that would include the human need for profit, responsible profit making, as you said, is what makes the free enterprise system motivating and rewarding, and makes people successful, as they aspire to be in this country, and that's part of what has collectively has produced the greatness of our country. But when some are exploiting that and taking that opportunity for profit making from people like yourself that's when the system breaks down.

MEADOWCROFT:

Do like Bill Gates Does when he puts money back in to our society billions of dollars. It's not that much money to them. But to make our society work it could work.

PRYOR:

Consistently people are writing in about high gas prices and they are telling stories about how stations have really increased prices dramatically over a very short period of time and they have a lot of stories. I think that one thing that is hard for people to stomach is when they go to the gas station and they pay a record high price to fill up their tank, then they open the business page and they see that the oil companies are making record profits. I think that's just very hard for people to understand. It's very hard for me to understand, so I am glad you all are here today to talk about this, and Mr. Meadowcroft, what I would like to do if possible is kind of focus on you here for just the next couple of minutes. It sounds to me like your like a pharmacist. People come in to a pharmacist. They complain about the high cost of medicine and drugs, but really the pharmacist probably makes a small profit off each thing they sell and that profit margin really does not change, is that fair to say with you and gasoline?

MEADOWCROFT:

Oh yeah, we are representing the industry really to the consumer. We've got the pump out there, and we are the farthest down the line so we do catch the heat.

PRYOR:

But in other words, your profit margin per gallon really doesn't change a whole lot, I assume, if gas is selling for $1.25 a gallon or for $3.25 cents a gallon.

MEADOWCROFT:

I really thought, being in the business, that when gas went three dollars a gallon, I'd be making more than 10 or 15 cents a gallon, I thought I'd be making like three times that. But it has not proven that way. When I was in business 40 years ago and you got three gallons for a dollar, I did better profit wise than I do today.

PRYOR:

Rights.

MEADOWCROFT:

Here it is 2005 and I'm still working on that 10 to 15% margin on three dollars. When you're taking about percentages, you're talking about 10, 15 cents on three dollars. You can't really survive in a business where its three dollars and you're making 15 cents. When it's a dollar, it's feasible. I've been going downhill for the last four or five years.

PRYOR:

Let me ask this question, in your store, it sounds like you sell some convenience store items as well, are you starting to see price increases on those items because of the fuel costs it takes to bring those items to your store?

MEADOWCROFT:

Not only that, but just because we've had so many hurricanes this year, everything you can think of has gone up, anything you buy – even a cupcake – costs you more because of the gas increases. But it's so much more than just gas increase, it's going to be every kind of commodity you have, because anything with plastic is going to cost a lot more, and a lot of our industries. Everything's made with plastic.

PRYOR:

Let me ask you about your industry specifically. Is there any one of the oil companies that are cheaper day in, day out, on their price of gasoline, or are they all about the same?

MEADOWCROFT:

I really think they're all basically the same. You have some large independents like Sheets, where they buy billions of gallons at a time, or Rudders, which is up my way. They've been cheaper because they already had a commitment like 2 or 3 months ago where they bought maybe 10 billion gallons. I go every three days where I have to buy gas, so I have to go through the process where they get allocations. You see some price difference there, where on the commodities market they actually buy futures, so those type of people can keep the price down, in which they have done.

PRYOR:

Now what town are you in in Maryland?

MEADOWCROFT:

I'm in Maryland, right on the Pennsylvania line.

PRYOR:

Ok, I'm just not familiar with that region of the country in terms of the refinery situation. The gas you sell in your store, where is it typically refined?

MEADOWCROFT:

Louisiana. (Laughs)

PRYOR:

Ok, so they pipeline it all the way up here.

MEADOWCROFT:

Pennsylvania, they have two pipelines coming up, one in Pennsylvania which is in Philadelphia, and then you have a pipeline—the colonial pipeline—that comes to Baltimore city itself. I'm in Baltimore county – their pipeline stayed open, and ours was actually closed down for a while and that's where the scare tactic came in and got everyone really scared and they ran out and loaded up with gas, which was the worst thing they could have done, but of course we all do that.

PRYOR:

Can you get fuel off the other pipeline?

MEADOWCROFT:

No sir. I'm not allowed to because Maryland has environmentally-corrected fuel, which costs like 10 cents more a gallon and I used to have drivers from Pennsylvania, but they couldn't deliver to me because of the additives put in the fuel that are state-regulated and they didn't have the facilities or the capabilities to do any of that. It had to go to Baltimore, come through the pipeline, and then there right there at Urban Avenue in the middle of Baltimore city, and the additives…

PRYOR:

…that meet the Maryland standards are added. So Maryland has a special set of standards…?

MEADOWCROFT:

Maryland has a special everything. It's especially high in taxes.

PRYOR:

That's a matter for a different hearing I think. (Laughter) But something you said in response to Senator Dorgan's question a moment ago, and you mentioned it here a moment ago with me as well. You said you get an allocation of gas, the gas is allocated to your station. Tell us how that works.

MEADOWCROFT:

Only in a tight market, see. The branded companies love stations like mine when they have an excess because then I move it. So when we have a tight market like it is now, they get gentleman, called "jobbers," and they get so much gas, before they used to get an unlimited supply, but as soon as things get tight, then they're allocated, then a jobber says to me, "I can get you this gas" – and this is really ridiculous – Before I used to call up and order gas and I'd be told what my price is. Then the guy puts the fear factor on me and tells me I only have allocations for 4 loads, so if you want this gas, you have to tell me that you're going to buy it and I'll tell you what the price is when you get it. And then I have to pay for it on the spot – where before I used to have three or four days to pay for it and I'd know what my price is. And that's how I got in this quagmire – this $3.49. I would have never bought it at $3.49, when up the road they're selling gas at $3.18, but I made a commitment to buy it, and I'm caught.

PRYOR:

Let me ask this along that same line there, I assume that when you sell gas at your station, you have a big sign up there with one of the big oil company's names up there?

MEADOWCROFT:

No, it's unbranded so I have no name.

PRYOR:

Ok, I was going to ask that. So you don't have a marketing agreement with anybody like Exxon, or BP, or anybody?

MEADOWCROFT:

No.

PRYOR:

It's up to you to buy your own gas.

MEADOWCROFT:

Right, that's where my problem lies now. It's great when things are great, but when things are tight, I'm left out in the cold.

PRYOR:

Let me ask this other question, and this is the last question I have, Mr. Chairman. Where you are, in your market in Maryland, the wholesaler that you purchase it from, is that the same as the refiner? In other words, not to pick on Exxon, but if Exxon is the refiner, does it go through an Exxon wholesaler? Is it intergrated?

MEADOWCROFT:

Yes, sir, that's basically what it is. They have "jobbers," or wholesalers, or whatever you want to call them, they have contracts with three or four different – some of them just work strictly Exxon, or strictly Shell – a couple of mine are that way – and a couple of the other ones have three or four branded companies or have them all, and they actually represent these companies with their excess supply, I mean that's what I feel it amounts to, I don't know if it's really true, but they keep their bottom line looking good because they have this excess and if they don't move it, of course, then it jams up the whole pipeline. So if America really wants to do something in this country that would be outstanding, and I'm in the gas station business myself, and it would hurt me for a few days, and I'd rather get hurt for a few days than for a week, if everybody would just quit buying gas, you'd be amazed at how it would change the whole picture, because if the gas don't flow, there's no money to be made. And it's really that simple.

So like they were saying on TV, on FOX news, if people would just quit buying gas one day a week, you would be amazed how this would send jitters through the whole industry. What I don't like about the oil industry is the idea that a man with a pencil determines price. Everyday he writes down what the prices are and he determines price. The way I've looked at it for 40 years. I might be wrong, this is the impression I get. It has no basis in reality. It has no basis at all what happened with Katrina, in reality, that our prices went up 40%. It has no basis is reality. Where did he come up with these figures?

PRYOR:

Mr. Chairman I think that's the point you're trying to make with these hearings. Thank you.

DORGAN:

Senator Pryor, thank you very much. Before this panel concludes and I call the other two witnesses, I should mention that since we began about an hour ago, it's about 9.5 million dollars of windfall or excess profits above record profits that the industry had already experienced. Figure that for 24 hours a day and you're talking about $240 millions a day in excess or windfall profits. That is the gain for the industry and the pain for the consumer. Again, these are profits above that which was already recorded as record profit levels in the year 2004.

Let me thank all three of you for being here and we appreciate very much the statements you have made and the contribution to the record you have made, and the discussion about oil and the price of gasoline. Thank you very much.

Next we will call on Mark Cooper from the Consumer Federation of America and Dean Baker, from the Center for Economic Policy and Research.

I would like to introduce both: Mark Cooper is the Director of Research at the Consumer Federation of America, where he has responsibility for analysis and advocacy in the areas of telecommunications, media, economic, and energy policy. He is a Fellow at the Stanford Law School Center for Internet and Society, and a Fellow at the Donald McGannon Communications Center of Fordham University.

He is the author of numerous books and papers including, *Equity and Energy*; *Media Ownership and Democracy in the Digital Information Age*; and others too numerous to mention.

Finally, Dean Baker, Center for Economic and Policy Research, is an economist and Co-Director of the Center. He previously worked as a senior economist at the Economic Policy Institute and an assistant professor at Bucknell University.

He has also written many books and articles, again, too numerous to mention. Worked as a consultant for the World Bank, the Joint Economic Committee of the Congress, and the Organization for Economic Cooperation and Development.

Let me thank both of you for being here and Mr. Cooper, on behalf of the Consumer Federation of America, you may proceed.

COOPER:

Thank you Senator Dorgan, Senator Dayton, Senator Pryor. The statement I give you today, I gave word for word at the House Energy and Commerce Committee a couple of weeks ago and it in fact draws almost entirely from a report we did in July of 2001, in which we looked at the structure of this industry and we raised some concerns.

Our central conclusion was that public policy cannot prevent accidents or catastrophic acts of nature. But it can build systems that are resilient, robust, and flexible to minimize the impact of the inevitable accidents in this kind of industry. It is evident that the business practices of the oil industry have combined, with the lack of a public policy in this country, to create a gasoline sector such as has difficulty coping with even minor events, not to mention a major disaster that struck the Gulf Coast last week. If the measure of performance of an economic sector is adequate supplies at stable prices, then this industry has failed the consumer, not just in the wake of Katrina, but also repeatedly over the past five years.

A typical household will spend in 2005 $500 per year more for gasoline than they did in 2002, and $750 per year more than they did in 1999. Those prices are strangling American households.

When we looked at the industry back in July 2001, we urged policymakers to aggressively move in five areas, and we gave specifics:

We must restore reserve margin in the gasoline sector by both increasing efficiency of our vehicle fleet and expanding production. Yes. We were for re-opening refineries. 50 refineries were closed over the course of the 1990s as business decisions that came out of oil companies that were merging. Those were sites that were full environmentally approved, the refineries were up and running, and they were shut down as a business decision. They remain closed as a business decision. The industry has failed to build refineries as a business decision. They like tight markets because it increases their profit.

We urged policymakers to increase the flexibility of the industry through expanding stocks and storage. Refineries run at 95 or 97%. That's far too high capacity utilization. Most industries in this country run at 85%. In the electric utility industry, this is a similar biocommodity with an inflexible system – capital-intensive. There's a reserve margin requirement of 15-20%. The oil industry acts irresponsibly by trying to operate at 95 or 97%. They do not keep stocks in the ground.

When our European allies in the International Energy Agency offered to help us out of our bind, they offered to use stocks from their strategic product reserve so they could get quickly into the gasoline tanks of Americans. We don't have a strategic product reserve in this country. We have a strategic crude reserve, but if you have a bottleneck in refining, then all that oil in the ground or in storage doesn't do you any good. So we need a policy that requires people to have more stock on hand. The industry calls it "just in time delivery," but in the oil business, "just in time" means "never there when you really need it." We need a much more flexible system. We need a more competitive industry.

Every refining market in this country is concentrated. Every wholesale market, a state-level market, is concentrated. Every retail market is concentrated, by the standard definition of the Department of Justice and the Federal Trade Commission. Now they have approved these mergers because they have a theory that says it shouldn't matter, but in fact, the GAO did a study last year, only through 2001, and found that it does matter. So we have an industry that is too concentrated and we need more competition.

And finally we need a policy that addresses the needs of lower income households. The typical low income household that has a car in this country will spend

10% of its income on gasoline this year. 10%. That's up almost 2 percentage points as a result of recent rising prices. The burden is too heavy.

We were living on a razor's edge. Consumption was increasing, capacity utilization was increasing, stocks were not expanding. Katrina pushed us off that edge. But Katrina is only the last of the series of incidents in which we constantly hear people – we hear the same refrain year after year, stocks were low, refineries were stretched to their limits and something happened. If it happens once, it may be a surprised. Twice, may be bad luck. But by the third time when the same thing happens, it's policymakers and the industry who are failing to react and respond to build a system that protects consumers from the abuse of market power, the failure of socially responsible policies to protect the public.

So as I urged the House Energy and Commerce Committee a couple of weeks ago, I urge you to take a different direction, to look hard at the policies in this country, to build by regulation – because this marketplace just doesn't work – to build a flexible, robust system that has spare capacity, the ability to respond to accidents which will inevitably happen, and protect the consumers from the abuse of market power. Thank you.

DORGAN:

Mr. Cooper, thank you very much for your testimony. Next we will hear from Dean Baker of the Economic Center for Policy and Research. Mr. Baker, you may proceed.

BAKER:

(Inaudible)

…getting pipelines and refineries up and running. The first point on windfall profit tax, the basic argument, you had begun by referring to a year, year and a half ago when oil was 40 a barrel, I'd actually go back a little further, if we go back to 2002, oil at that time was $25 a barrel. If we go a little further back, 1998, it actually had fallen as low as $15 a barrel, but the point here is that the oil industry was prepared to make a profit selling its oil at $25 a barrel. If you go back in 2002, it wasn't anticipated, or at least, not widely anticipated, that we'd be seeing oil at $60 and $70 a barrel as we have recently.

Secondly, obviously we've had a run-up in refined products in the wake of Katrina, apart from the run-up in crude, which again, presumably, was unanticipated, and Mark has gone through the backdrop for that – the shortage of capacity. But again, long and short, we had the industry prepared to sell profitably home heating oil and gasoline at prices far, far below what they're actually getting. Again in this situation, due to an unanticipated shortage, and this has shown up in the industry profits, which we have going here…

(Points to profit monitor)

…but just to give you another take on that – I don't have it broken down by company – but if we just look at the national income and product accounts, I got the numbers for the first quarter because the second quarter is not yet in, industry profits were running an annual rate of $62.8 billion in the first quarter, and this is just their domestic profits, and that compares to an average of $24.3 billion (adjusted for inflation, so I like to do honest numbers) over the prior five years, so we're looking at $62.8 billion in the first quarter. We all know it'll be much higher in the second and third quarter, compared to $24.3 billion, as an average, over the last five years. In other words, profits have gone up roughly 150% just as of the first quarter, and clearly we're talking about them going still higher.

Now, the idea about this being a windfall, the industry has done nothing, it's not as if they've developed great new products or people have suddenly gotten an urge to buy their gasoline that they hadn't had previously. We all know it is simply a case of having bad luck in the case of Katrina, bad luck in the case of some unexpectedly rapid rises in demand worldwide, party to the growth in China and some other unexplained factors, and partly due to the loss in oil production from Iraq.

All factors have driven up prices worldwide, which has meant bad luck for the rest of us. The panel that was here earlier talked about the bad luck, how that's manifested in their lives, their businesses, and we all know this is a huge problem for the country. But obviously what is a problem for the country is a great gain for the oil industry.

The logic of the windfall profit tax is to take back part of that gain. The idea is that the industry did nothing for these profits, they're happy to get them, I understand, if I were running Shell, I'd be very happy to tell my shareholders that I have billions more to give you this year, but the fact is, they didn't do anything for that and I would say that the people in this country probably could use that money more wisely than the shareholders of Shell Oil Company.

So the logic of the windfall profit tax is you set some platform, what I said in the paper that I submitted to the committee in my testimony was I said we set a platform of 10 percent above their average profits over the last five years, they were doing just fine previously, at least that's what they are telling their shareholders, and then we say we tax away a certain portion, 30%, 40%. If we go back to the early 80's the tax got as high as 70%. But the point is that this is money that they weren't counting on, they didn't do anything for and could be much better used say as a rebate for consumers, help in the recovery of Katrina. There is no shortages of need for that money. It could be better used in public hands than in the hands of the shareholders of Exxon-Mobil, Shell, the other oil companies. A basic comparison, there are differences between now and going back to the early 80's, but the windfall profit tax during those years, 81 to 83, raised an amount of revenue that was just shy of 6/10ths of 1% of GDP, that would be about 70 billion a year right now. So we are talking about a lot of money that doesn't in any fundamental way jeopardize the supply of oil, the conduct of the oil companies. They were not counting on this money. They are not going to use it to drill for more oil. It's simply money that will be dispersed to their shareholders.

The second point I wanted to make just again referring to comments Senator Feinstein made earlier, we know that there is capability to abuse the system here. The disaster of Katrina provides a prime opportunity that we saw damaged pipelines, damage to refineries, and I hate to say this that we have good reason to believe that the industry is going to take advantage of that to push up prices. In other words, they all recognize that by virtue of a pipeline being off line, by virtue of a refinery being offline, they can charge more for their product. They are better off not having them online than having them online. And we don't have to go to ancient history, as Senator Feinstein pointed out, we know they did exactly this in the energy shortage in California in 2001, and unfortunately the agency, the Federal Energy Regulatory Commission, that responsible for making sure that did not happen, was actually going out telling the public that something like that could not possibly occur. With the collapse of Enron, we found out that that's exactly what was going on, and that they had developed this to an art.

So I just conclude by saying that it's very important that we have diminished regulatory tools today to deal with this, and so far as we have regulatory tools we have to use them. The public has to monitor this and we have to be aware of the fact that it's very likely that the energy companies will take advantage of this disaster to try to push up prices still further and in that way get ever higher profits. So I'll stop there and take questions.

DORGAN:

Mr. Baker thank you very much. Mr. Cooper thank you for your testimony. I, by accident, driving down the road the other day, on my car radio, got one of these talk radio shows, that attempt to portray deep sounds from the chest, as thoughtful emotions from the brain. They don't do it very well, but that's their attempt.

And one of the things that they said was that the reason we have an energy problem, the reason for the crisis situation is because we closed down all the refineries, all the environmentalists closed down all the refineries, or at least prevented any additional refineries from being built, and so the oil companies didn't come here today, but let me just ask a question perhaps as they might over a bottle of green belt and hypothesize over what your testimony means. They would say, "You're a couple of hot shots with some big college degrees. You're wearing suits that cover your tree-hugging hearts, and you're the problem, not the solution, and your analysis of it misses the point that the environmentalists have prevented this country from having more refineries and that's the problem, end of story, shame on you." So what's wrong with their assessment here?

COOPER:

Actually you can go back to the Federal Trade Commission's investigation of the first price spike of the new millennium, which was the price spike in the Chicago market in 2000. And Chairman Petovski did a detailed investigation and what he discovered was that there were three refineries serving that market and each of the refiners decided when they reconfigured their refineries, as a business decision, to reduce their output, and they were complying with the Clean Air Act, but this was a business decision, to reduce their output and cut off their independent distributors. You heard that problem from the gas station owner.

So the Chicago market ended up with 23% less refining capacity servicing that market as a result of a business decision. The 50 refineries that were closed right after the mergers were all business decisions. Now they took certain things into account, but they closed those refineries as business decisions, they expanded some, but they've never gone back and reopened those and that's why in 2001, when we entered into this fray—this is just the start of it—we identified those sites and we asked Congress to do a simple thing: catalog those sites, study those refineries, understand why they were closed, and figure out how to get them reopened.

The Saudi's have offered to build two refineries in this country. They'll put up the money, but it's a business decision. So they're certainly making an immense amount of money in the refineries they kept open, but they have no economic interest in expanding capacity.

In a competitive market, if you run out of product and the other guy still has product, he or she will steal your business. That can't happen in the oil industry, and so they don't have the discipline of the market forces to keep adequate surplus production and storage on hand to protect themselves from competition because there is no competition from which they need protection.

DORGAN:

First of all, I didn't do a very good job of mimicking the prevailing winds of talk radio, so I shouldn't have tried to do that, but the point you just made, Mr. Cooper, is underscored by something that I picked up – just released in fact a while ago – a group called the Foundation for Taxpayer and Consumer Rights had been able to extract memorandums – and these memorandums come from the 1990s – internal memos from Mobil, Chevron, and Texaco, that show different ways the oil giants closed down refining capacity and drove independent refiners out of business.

For example, this quotes an internal Chevron memo, it's from the 90s, "a senior energy analyst at the recent API convention warned that if the U.S. petroleum industry doesn't reduce its refining capacity, it will never see any substantial increase in refining margins."

It then discusses how major refiners were closing down their refineries. A Texaco memo disclosed how the industry believed that the most critical factor facing the refining industry on the west coast is the surplus of capacity and the surplus gasoline production capacity and it described the events that need to result in changing that.

In fact at the Energy Committee we did have a hearing, we didn't have the energy companies there, but we had the experts there, other experts, and they've said the exactly the same thing that you have said Mr. Cooper , Mr. Baker, have said "Why are there not more refineries or why is there not more refining capacity?" and the answer is it has to do with rate of return, and the industry believes it has too low a rate of return and we don't have more refineries built.

But if you listen to talk radio and other venues and my other colleagues in Congress they'll say the reason we don't have more refineries is that it's the environmentalists, which is not the case, but that's the case that is made.

Mr. Baker, do you agree with Mr. Cooper with respect to the dramatic concentration of the oil industry and its impact on the so-called free market.

BAKER:

I think that is certainly a key part of the story and that shows up in the refining sector. The argument would be, the reason why you'd keep excess capacity is that if there were ever a shortfall, you don't want your competitors to run out there and steal away your market share. Clearly they don't have to worry about that since it's become such a concentrated industry. That's not a realistic fear, so he's exactly right in that respect.

The other part of the story, I do have to say, in terms of the run-up in prices in the wake of Katrina is in refined products. But the underlying run-up in crude oil prices, that's an issue that, again I wouldn't say it's a free market issue necessarily, but that is a worldwide market, and that's an issue that, if we look at worldwide supply and demand, we have seen rapid growth in demand and there are, I wouldn't say absolute limits in the sense that we're not about to run out of oil tomorrow, but there's a limit to how rapidly you can bring oil online, so I'm not sure to what extent the concentration in the industry has been responsible for the run-up in crude oil.

DORGAN:

Mr. Baker, let me just make a point, and Mr. Cooper wants to respond to it as well. I accept the notion that we're going to have a greater increase in demand for oil and the products that come from oil. China now has 20 million cars in a country of 1.4 billion people. It's estimated that 20 million cars will grow to 120 million cars by the year 2020.

What does that mean for the dramatic need for increased energy for China? It's obvious what that means for the demand side of that supply and demand curve. But understanding all of that, if you just go back to the week before Katrina hit, which I think is the most important part of this hearing, before Katrina hit, we had seen a substantial run-up in the price of oil and gas.

We listened to it every morning—what's the price of oil, what's the price of gas—and that had nothing to do with the natural disaster at all. That I think had to do with the three things I had mentioned before. One, internationally OPEC ministers sitting around deciding in their interests what they want to produce and how they like to price it. Second, excessive speculation in the futures markets. And third, an increased concentrated industry through dramatic mergers that have left this to be much less of a free market.

Your response, Mr. Cooper?

COOPER:

We've actually looked at this question of the split between crude and what's called the domestic spread. Essentially you calculate the domestic spread, you've got the pump price, you take out crude, that's set politically by a cartel. There should be no pretense that that's a marketplace, because those guys sit together and they decide capacity and they decide production in a semi-public meeting. That's not what any market I ever read about in Adam Smith, although he always said that whenever capitalists get together they immediately talk about prices. So we look at the domestic spread, which is take out crude, take out taxes, and then look at what's left. That number, if you go back the August before Katrina, was up by about 25-30 cents a gallon compared to the 1990s.

Now crude oil is probably up 50-60 cents a gallon at that time and I understand that the 50 cents a gallon matters a lot, and that's an OPEC problem and we ought to do something about that. But the 25 cents a gallon matters also and that's what the oil industry accomplished by implementing the strategy you identified in those memos. They set out the tight net market to eliminate the independents and they increased their profitability by 25 cents a gallon on domestic spread.

So about a third of the increase, and that's domestic companies doing things to American consumers. That's within our control, and we haven't done anything about it in the four years since we flagged the problem.

DORGAN:

Senator Dayton.

DAYTON:

Thank you Mr. Chairman. We heard testimony just before you from Mr. Meadowcroft that the refineries charge his independent gas station more money for gasoline than they charge the stations that share their brand names. Would you support legislation that would require refineries to sell the gasoline to all stations, branded and independent, at the same price?

COOPER:

The problem he described in Maryland occurred in Texas, that was where the witnesses were on the House side. There was a 40-80 cent per gallon difference between the branded and the unbranded. What that does is create a tremendous amount of headroom, for a problem for the unbranded guy, he's out of the gasoline business effectively. So that's a form of price discrimination.

In the old days, there used to be independent refiners who would discipline that abuse. They don't exist today. We have to do something about it. There's no doubt that the refiners took the first bite in the week after Katrina. They put up their price a tremendous amount, especially to the unbranded guys. That is the abuse of market power, we need to do something about it.

DAYTON:

Mr. Baker?

BAKER:

I'd just caution on that, you may want to do that, but I would just point out the flip side of that. Mr. Meadowcroft, I think, referred to this earlier during his testimony, that during normal times, he could often get a good deal and probably pay somewhat less than his branded competitors. So what you would be doing if you require that they charge the same price to the branded and non-branded is you would be cutting him out during those good times. It may be something you want to do, but I would just caution you.

DAYTON:

Good point, thank you. Mr. Cooper, in you're written testimony you state, and I wonder if you'd elaborate, "regrettably just last month the Department of Transportation proposed timid improvement in fuel efficiency standards, gerrymandered the calculations to let more gas guzzlers escape scrutiny, and exempted some of the worst gas guzzlers from fuel consumption standards altogether." How do you gerrymander the calculations?

COOPER:

What you do is fuss around with how you're going to average out the different vehicles. We have one way of averaging it and then what happened was you move vehicles into certain categories and you make it a little bit easier to hit the target by shifting it around. That's just like gerrymandering, you move the district around and make it a little easier to get elected.

But let me make just one fundamental point about that document. When it came out I saw it and then along came the hurricane. In order to arrive at this piddling, embarrassingly timid increase in the fuel efficiency of light trucks, the Department of Transportation used, as the social cost of oil, in 2011, including taxes, a figure of $1.80 a gallon. That number is economically irrational and socially irresponsible.

Oil is much more valuable to this country than that. Not in the pump price, because we complain about the pump price, but there are hidden social costs that we really do have to think about. We have the economic slowdown which we're going to get, we have geopolitical vulnerability, we have a trade deficit, we have currency instability, and we have environmental problems. All five of those things do not turn up in the pump price. They are social issues – public policy problems – that ought to be in the planning process, if not in the pump price. That figure that they used was an embarrassment to anyone who wants to seriously think about energy policy in this country.

DAYTON:

Thank you. Mr. Baker, did I understand you correctly that you said in 2002 the price of oil was $25 a barrel and that was profitable to sell, obviously it was, but by my simple calculation, given the price at $65 a barrel, is that $40 a barrel of essentially windfall profit?

BAKER:

It will be windfall for someone, I should point out, in some of these cases, you'll have U.S. oil companies who are buying from foreign producers, from OPEC, and most of that money might be going to Saudi Arabia, Venezuela. Of course in some cases they have long-term contracts where they might have locked in crude at maybe $20 a barrel for three years, four years, five years, so they're still paying that if they locked it in back in 2002, in which case yes.

DAYTON:

Then it's somebody's profit…

BAKER:

It might not be Exxon-Mobil. It might be Saudi Arabia.

DAYTON:

Good point. I'm having trouble keeping up with Senator Dorgan's…

BAKER:

If I could actually comment on the gerrymandering because I'd actually take an even stronger position than Mr. Cooper, that if you go back to the whole origin of the distinction between light trucks and cars, the whole point, when we first put in the CAFÉ standards back in the 1970s, the argument about having no restrictions on light trucks was that these were business vehicles. You had small business owners, and you had farmers who needed these light trucks, so you weren't going to regulate their standards.

In the 1980s of course, we know that came to be applied to SUVs, minivans, all these things that are clearly for not business purposes in a vast majority of cases, so this was extreme gerrymandering. I think he's understated the case.

DAYTON:

Going back to windfall profits, because I can't keep up with that number over there escalating, do you have an estimate, either of you, of what the windfall profits were for the oil industry in 2004, or say, today in 2005?

COOPER:

We actually did those numbers through 2004. Again we started in 2001 because that's when we started getting the problem, and we concluded that before tax profits, you were looking at an increase of $150 billion from 2000 to 2004, and that's the cumulative total.

You will be up well over $200 billion of increased before-tax profits, because I do it before tax because that comes out of my pocket. They always do it after tax. The before-tax profits are in the pump price. So we are looking at well over $200 billion.

Let me add one other point about the windfall. Dr. Baker described a variety of ways to think about it, but the most interesting way to think about it is that the oil companies today, still behave in their investment decisions, and the *Wall Street Journal* has complained about this, the International Energy Agency – as if they think the price of oil is going to be $25 a barrel. They're making investments only up to that number. And that tells you that if you tax anything away above that number, you will not have any impact on the efficiency of the industry.

And that's an important point about these sorts windfall profits because they don't elicit efficient responses, and they're still behaving – and they said "we got burned in the past when we increased our investment…" But you know what, it's an interesting point, we all know that the definition of a competitive market is being a price-taker. You can't be a price-maker, you're supposed to be a price-taker.

In a competitive market, you're supposed to be an investment-taker too. You're not allowed to pick and choose what investments you want to make. You're supposed to be whipped by the market into pursuing every available opportunity. You don't get to play around at $25 a barrel when people are getting $60 a barrel. That's the best indication that there's a windfall there that you can tax away without hurting the efficiency of the industry. They're not using it, they're not putting it to good purposes.

DAYTON:

Mr. Chairman, I just want to conclude by saying we just appropriated, by necessity, almost $63 billion for Hurricane Katrina responses and that's going to escalate in the next couple of weeks. This windfall profits tax would certainly be a better way of paying for part of that than putting that burden either on the American taxpayer now or on our children and grandchildren later. Thank you for holding this important hearing.

DORGAN:

Senator Dayton, thank you very much. I just want to make a final point. My colleague from California, Senator Feinstein, talked about what California faced with respect to the wholesale markets for electricity. Many of us, myself included, in my committees were pushing to try to come in and do something about price controls. They all said "nonsense."

We now discovered that what had happened in California and across the west coast was a vast criminal conspiracy. There are people going to prison who stole money from millions, tens of millions of people on the West Coast.

While we were trying to get people's attention to this, the policymakers, the Secretary of Energy said that suggestions of price conspiracies were "myths."

Vice President Cheney derided "politicians who want to go out and blame somebody and ledger some kind of conspiracy."

Charles Krauthammer in the *Washington Post* suggested that "only silly Californians think that rolling blackouts are a conspiracy by the power companies to raise rates." In fact, Krauthammer said, "politicians are thundering, fingers are wagging, and complicated theories are being hatched, while the problem was simply that demand was up and supply was down."

William Safire in the *New York Times* warned against "populist interference" with the energy market's "self-correction."

There is of course no truth in labeling for pundits, in this town, or anywhere else for that matter. They can be wrong and consistently wrong. It doesn't matter. They keep writing. They buy ink by the barrel and they just keep writing and giving us their missives.

I'm not suggesting that there's a parallel here. I'm only saying this: those of us who saw what was happening on the West Coast made an early warning about it and it was largely ignored by these people, including President Bush.

This was the market system at work? It was not, it was not at all. The wholesale electricity market in California was manipulated by people involved in criminal behavior and some of them are going to go to prison.

Whenever we have any markets that are not free markets, where you have participants in a marketplace who have the ability, the sheer, raw market power and muscle to price as they wish, then you have a perverted system. That's where you need government regulators to go to work.

The Federal Trade Commission is required by the energy bill signed by the president, a provision I put in the energy bill, to launch an investigation within 90 days of the president's signature, of energy pricing of oil and gas.

I must confess, I hold very little confidence in the Federal Trade Commission not wanting to do this in an aggressive way, will do much of a job. But I think that we must, through all kinds of devices, including hearings like this, raise the flag of great concern about what's happening in these marketplaces, who's gaining, and who exhibits the pain.

I think, Mr. Cooper, Mr. Baker, your contributions are very helpful to us. Obviously your contributions are somewhat practiced because I get the sense that you have spoken about this before, probably repeatedly, and you two are sounding the warning about the need for a free market, and when a free market doesn't exist, the need for effective regulation to protect the consumers.

I think, one final point. All of us believe we need to find new sources of energy. I hold no grudges with the energy industry. We produce oil in North Dakota. I want those that produce oil and gas to have an adequate return, a fair return, the kind of return that will persuade them to make additional investments to find additional supplies. I want that.

But I also believe on behalf of America's consumers that what is happening with pricing today is a perversion of the free market system. Congress and the president need to act in my judgment. Let me thank Senator Dayton.

DAYTON:

Can I just concur with you Mr. Chairman. This country was founded on populist interference against economic exploitation, and it's called the Boston Tea Party. It continued from there and about century ago, a Republican president, Theodore Roosevelt, went after the trust-busting, those who were exploiting the people of this country.

We are so far away in this body, regretfully, as we know, being in the minority, the majority instinct here is so far removed from anything that would stand in the way of this kind of profiteering and exploitation.

Mr. Safire and others need not have a shred of concern, unfortunately, because this body is constituted by the majority, and the House as well, and this administration, the sky is the limit. Anything that is taken out of the pockets of the consumers, however unjust, with the kind of impacts we heard from real people in their lives, multiplied by hundreds of millions around this country, is irrelevant to most people here. Despite an occasional lip service, there's nothing being done about it.

DORGAN:

Senator Dayton, thank you. We will again continue our request and when and if oil company executives wish to come and provide their story, we would be very happy to reconvene the hearing. As always, at these hearings, and any future hearing on energy, we will invite our Republican colleagues to come and join us as well. These issues are not Republican or Democrat issues, they are issues important to the future of this country.

Mr. Cooper and Mr. Baker I think, both, have identified substantial, serious economic problems we face in this country that are not being stared directly in the eye by people in town that should. So we will continue to try to call attention to them through these kinds of hearings.

Thank you very much for appearing. This hearing is adjourned.