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Real Help for American Consumers: Who's Profiting at the Pump?

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**REAL HELP FOR AMERICAN CONSUMERS:
WHO'S PROFITING AT THE PUMP?**

**Democratic Staff
Committee on Oversight and Government Reform
U.S. House of Representatives**

Prepared for Ranking Member Elijah E. Cummings

May 23, 2011

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EXECUTIVE SUMMARY

With gas prices now at more than \$4 per gallon, Rep. Elijah E. Cummings, the Ranking Member of the House Committee on Oversight and Government Reform, asked minority staff to examine the fundamental causes of recent price increases. Staff reviewed the work of ten different congressional committees, including the Oversight Committee, and analyzed data and information from a number of experts, including industry representatives, government officials, and academics. This report presents the results of this review.

The report's chief conclusion is that, in order to make the most significant impact on lowering gas prices, the Committee's primary focus should be on countering the growing impact of excessive speculation, rather than pursuing the oil industry's priorities of increasing domestic drilling or repealing safety measures put in place after the devastating BP oil spill. Experts estimate that excessive oil speculation could be inflating prices by up to 30%, while increasing domestic drilling would impact prices by only about 1%, and then only after a decade or more. Addressing excessive speculation offers the single most significant opportunity to reduce the price of gas for American consumers.

The oil industry is the most profitable in the world.

Despite the worst economic crisis since the Great Depression, oil companies have continued to make the highest profits of any industry. The top five oil companies have enjoyed profits of nearly a trillion dollars over the past ten years. They reported profits of more than \$31 billion in the first quarter of FY 2011, more than 32% higher than in the first quarter of FY 2010.

Yet oil companies continue to benefit from billions of dollars in tax subsidies, as well as special deals that allow them to drill on federal lands without paying royalties. The Office of Management and Budget estimates that eliminating unnecessary tax subsidies could save more than \$43 billion over the next ten years, and the Government Accountability Office reports that U.S. taxpayers may be foregoing up to \$53 billion in revenues from oil companies that drill in the Gulf without paying market-rate royalties. Both industry officials and their supporters in the House have expressed support for ending this preferential treatment:

- Former Shell CEO John Hofmeister said in February, "In the face of sustained high oil prices it was not an issue—for large companies—of needing the subsidies to entice us into looking for and producing more oil."
- House Speaker John Boehner said in April, "I don't think the – the big oil companies need to have the oil depletion allowances. ... We certainly oughta take a look at it. ... And they oughta be payin' their fair share."
- House Budget Committee Chairman Paul Ryan, when asked whether he supports ending tax subsidies for oil companies, said in April, "I agree. ... We also want to get rid of corporate welfare. And corporate welfare goes to agribusiness companies, energy companies, financial services companies. So we propose to repeal all that."

- House Oversight Committee Chairman Darrell Issa, when asked whether he supports requiring oil companies to pay fair returns on oil leases in the Gulf, said in March, “there is bipartisan support, still, to try to fix that.”

Despite these statements, every legislative effort to address these problems that has come before the House in the 112th Congress has been defeated.

Countering excessive speculation will have a direct impact on prices at the pump.

According to the U.S. Energy Information Administration, the price of oil has been hovering around \$100 for some time. Industry officials, regulators, and outside experts have determined that these prices are artificially high in part due to the increasing role of energy speculation in the futures market. They estimate that excessive speculation may be inflating prices by up to 30%.

On May 12, Rex Tillerson, the CEO of ExxonMobil, testified before the Senate Finance Committee. When asked by Senator Maria Cantwell how much a barrel of oil would cost without excessive speculation, he responded, “Well it’s pretty hard to judge but it would be, you know, when we look at it, it’s going to be somewhere in the \$60 to \$70 range.” Similarly, on April 11, Goldman Sachs warned its investment clients that speculators may be inflating the price of oil by as much as \$27 a barrel.

On March 15, Bart Chilton, a Commissioner with the U.S. Commodity Futures Trading Commission (CFTC), warned that the impact of speculators is increasing rapidly. He stated: “There are now more speculative positions in commodity markets than ever before. Between June of 2008 and January 2011, futures equivalent contracts held by these types of speculators increased 64 percent in energy contracts.”

The Dodd-Frank Act included provisions to counter excessive speculation, including enhanced authority for the CFTC to set position limits and raise margin limits. However, opponents of the Act, including Speaker Boehner and Chairman Issa, have sought to repeal Dodd-Frank in its entirety, cut funding to the CFTC, and delay implementation of these provisions.

Some industry experts warn that these actions could increase gas prices. According to the Executive Director of Gasoline and Automotive Service Dealers of America, “The fastest way to six dollar gasoline is to cut the funding to the CFTC.”

Increasing drilling and repealing safety measures will not lower gas prices.

In contrast to addressing excessive speculation, which may be inflating prices by up to 30%, experts believe that focusing on the industry’s priorities of expanding domestic drilling and repealing safety measures will have a negligible impact on gas prices.

The U.S. Energy Information Administration examined the potential impact of expanding domestic oil exploration and drilling on the outer continental shelf of the Atlantic and Pacific

coasts of the United States and the Eastern and Central regions of the Gulf of Mexico. It concluded that there would be no change in prices by the year 2020, and that there would be a decrease of only 3 cents per gallon by the year 2030.

Despite this evidence, some proponents of drilling have blamed the Obama Administration for high gas prices. On April 20, 2011, for example, Chairman Issa argued that the Administration's policy toward offshore drilling "has resulted in higher prices for gas." This echoed several statements by former Alaska Governor Sarah Palin. Numerous industry and other experts have repudiated these claims. For example:

- In January, Ken Green, a resident scholar with the American Enterprise Institute, stated: "The world price is the world price. Even if we were producing 100 percent of our oil, ... [w]e probably couldn't produce enough to affect the world price of oil."
- In March, Michael Canes, the former chief economist for the American Petroleum Institute, stated, "It's not credible to blame the Obama Administration's drilling policies for today's high prices."
- Also in March, Chris Lafakis, an economist at Moody's Analytics, stated: "There is absolutely no merit to this viewpoint whatsoever."

Critics also claim that safety measures put in place after the BP oil spill are harming local economies. These claims disregard the massive economic and environmental devastation caused by oil that gushed unabated into the Gulf for 87 days. The spill devastated the commercial and recreational fishing industries through closures—which at their peak amounted to nearly 37% of all federal waters in the Gulf—and through decreases in consumer demand for Gulf seafood. The spill also decimated the Gulf's travel and tourism industries, which represent 46% of the Gulf's economy, generate over \$100 billion annually, and are responsible for more than a million jobs.

Finally, critics have asserted falsely that the Administration has instituted a "permitiorium," or a de facto moratorium, on approving drilling permits in the Gulf. This claim appears to have been created by oil industry communications officials and repeated by Members of Congress. In fact, no such "permitiorium" exists. The Administration has approved 14 deepwater drilling permits, 55 shallow water permits, and two new exploration plans since the BP oil spill.

Initial delays in obtaining permits were a result of the industry's ongoing efforts to develop an adequate technology to prevent and contain exactly the type of blowout that caused the BP oil spill. On February 17, 2011, the industry announced the completion of a "subsea capping stack" to perform this function. Less than two weeks later, the Administration approved the first of multiple deepwater drilling permits issued since the BP oil spill.

I. THE OIL INDUSTRY IS THE MOST PROFITABLE IN THE WORLD

A. Oil Companies Are Making Record Profits

Despite the worst economic crisis since the Great Depression, oil companies have continued to make the highest profits of any industry in the world. On February 3, 2011, the Democratic Staff of the House Committee on Natural Resources issued a report finding that the top five oil companies have enjoyed profits of nearly a trillion dollars over the past ten years. Analyzing data from ExxonMobil, Chevron, ConocoPhillips, BP, and Shell, the report concluded that, from 2001 to 2010, these five oil companies had profits of \$952 billion.¹

Oil companies have continued to enjoy record profits during the economic recession while other industries experienced significant losses and ordered major layoffs. In the first quarter of Fiscal Year 2011, the top five oil companies reported profits of more than \$31 billion—a 32.6% increase over the first quarter of 2010.² Only BP—which had the most devastating oil spill in U.S. history—posted profits lower than in the same quarter last year.³

Figure A. Oil Industry Profits <i>First Quarter 2011 Increase Over First Quarter 2010</i>		
ExxonMobil	\$10.7 billion	69% increase
Shell	\$6.3 billion	30% increase
Chevron	\$6.2 billion	36% increase
BP	\$5.5 billion	2.1% decrease
ConocoPhillips	\$3.0 billion	44% increase
Total	\$31.7 billion	32.6% increase

¹ Democratic Staff Report, House Committee on Natural Resources, *\$1 Trillion in Profits and Still at the Trough: Oil and Gas in the 21st Century* (Feb. 3, 2011) (online at [democrats.naturalresources.house.gov/sites/democrats.resourcescommittee.house.gov/files/Oil%20Profits%20and%20Tax%20Breaks%20\(2-1-11\)3JD_JP_DW_FINV5.pdf](http://democrats.naturalresources.house.gov/sites/democrats.resourcescommittee.house.gov/files/Oil%20Profits%20and%20Tax%20Breaks%20(2-1-11)3JD_JP_DW_FINV5.pdf))

² *Gas Earnings: Exxon Profits Up 69%, Shell Up 30%*, KLPW Radio (Apr. 28, 2011) (online at www.klpw.com/content/gas-earnings-exxon-profits-69-shell-30); Chevron, *Chevron Reports First Quarter Net Income of \$6.2 Billion, Up From \$4.6 Billion in First Quarter 2010* (Apr. 29, 2010) (online at www.chevron.com/articledocuments/latest/news_204200/5968ad10-51ed-40c3-a6b6-043a46825a82/earnings_29April2011.pdf.cvxn).

³ *Senate Bill Squeezes Big Oil to Ease Deficit*, Reuters (May 10, 2011) (online at news.yahoo.com/s/nm/20110510/pl_nm/us_usa_bigoil_taxbreaks).

B. Oil Companies Receive Billions in Unnecessary Tax Breaks

Despite these record profits, oil companies continue to receive billions of dollars in tax subsidies that industry and government officials believe are unnecessary and have no effect on gas prices. In his State of the Union address on January 25, 2011, President Obama called for an end to these unnecessary subsidies. He stated:

I'm asking Congress to eliminate the billions in taxpayer dollars we currently give to oil companies. ... I don't know if you've noticed, but they're doing just fine on their own. So instead of subsidizing yesterday's energy, let's invest in tomorrow's.⁴

This is the same position his predecessor took six years earlier. In April 2005, then-President George W. Bush stated:

I will tell you, with \$55 oil, we don't need incentives to oil and gas companies to explore. There are plenty of incentives.⁵

Industry officials also concede that these tax subsidies are unnecessary. On November 9, 2005, the Senate Committees on Commerce, Science and Transportation and Energy and Natural Resources held a joint hearing with five oil company CEOs. When asked by Senator Ron Wyden whether they disagreed with President Bush's statement that oil subsidies are unnecessary to encourage exploration, they all responded that they did not disagree:

Leo Raymond, CEO, ExxonMobil: No, I do not think our company has asked for any incentives for exploration.

David O'Reilly, CEO, ChevronTexaco: Agreed.

James Mulva, CEO, ConocoPhillips: In my oral comments, I said we do not need. ...

Ross Pillari, CEO, BP America. He is correct.

John Hofmeister, CEO, Shell: Yes, he is.⁶

⁴ The White House, *Remarks by the President in State of Union Address* (Jan. 25, 2011) (online at www.whitehouse.gov/the-press-office/2011/01/25/remarks-president-state-union-address).

⁵ The White House, *President Addresses American Society of Newspaper Editors Convention* (Apr. 14, 2005) (online at georgewbush-whitehouse.archives.gov/news/releases/2005/04/20050414-4.html).

⁶ Senate Committee on Commerce, Science, and Transportation and Senate Committee on Energy and Natural Resources, *Joint Hearing on Energy Prices and Profits*, 109th Cong. (Nov. 9, 2005) (S. Hrg. 109-307) (online at frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109_senate_hearings&docid=f:26108.wais).

Since he left his company, former Shell CEO John Hofmeister has made clear that his position has not changed since his testimony. On February 11, 2011, he stated, “In the face of sustained high oil prices it was not an issue—for large companies—of needing the subsidies to entice us into looking for and producing more oil.”⁷

On May 5, 2011, the Office of Management and Budget (OMB) estimated the savings that would be generated by eliminating several tax provisions that result in preferential treatment for oil companies.⁸ OMB estimated that, from 2012 to 2021, eliminating these tax subsidies could save approximately \$43.6 billion. See Figure B.

Figure B. OMB Savings Estimate for Eliminating Oil Subsidies	
Proposed Action on Tax Provisions	Ten-Year Savings
Repeal expensing of intangible drilling costs.	\$12.4 billion
Repeal deduction for tertiary injectants.	\$92 million
Repeal exception to passive loss limitations for working interests in oil and natural gas properties.	\$203 million
Repeal percentage depletion for oil and natural gas wells.	\$11.2 billion
Repeal deduction manufacturing deduction for oil and natural gas companies.	\$18.3 billion
Increase geological and geophysical amortization period for independent producers to seven years.	\$1.4 billion
Total	\$43.6 billion

This month, the Congressional Joint Economic Committee issued a staff report calling for an end to tax subsidies for oil companies and finding that such action would not increase gas prices, as some have claimed. The report stated:

Eliminating these tax preferences, which subsidize fossil fuel production, will both reduce the federal deficit and expedite the transition to a cleaner-energy economy. Critics of repealing these subsidies argue that the targeted tax breaks spur production and lower energy prices. In reality, most of the so-called incentives have no impact on

⁷ *Ex-Shell CEO Says Big Oil Can Live Without Subsidies*, National Journal (Feb. 11, 2011) (online at nationaljournal.com/daily/ex-shell-ceo-says-big-oil-can-live-without-subsidies-20110211?print=true).

⁸ Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2012, Terminations, Reductions and Savings*, at 52 (online at www.whitehouse.gov/sites/default/files/omb/budget/fy2012/assets/trs.pdf) (accessed May 20, 2011).

near-term production decisions, and thus repealing them would have no effect on consumer energy prices in the immediate future. Even in the longer term, the current proposed changes to these tax provisions would have little impact on global production and a negligible effect on consumer energy prices. More importantly, these subsidies failed to prevent spikes in the price of gasoline, such as the spike that occurred in 2007-08. At the same time, these tax breaks may have discouraged investment in other industries, including alternative energy sources or energy efficiency, by distorting the effective tax rate on investments in oil and natural gas.⁹

A University of Massachusetts study issued in 2009 found that investment in clean energy sectors creates roughly three times more direct and indirect jobs than when the same amount of money is spent on developing carbon-based fuels. The study reported, for example, that investing \$1 million to retrofit buildings to make them more energy efficient creates three times as many jobs than a \$1 million investment in oil and natural gas.¹⁰

C. Oil Companies Make Billions More From No-Royalty Leases

In addition to obtaining significant tax subsidies, oil and gas companies benefit from special deals that allow them to drill on federal lands without paying a fair return on royalties.

The United States enters into leases with private companies to extract oil and gas from federal lands. In return, the oil and gas companies make payments to the federal government, and the Department of the Interior manages the collection of these revenues. In February, the Government Accountability Office (GAO) released its latest “High-Risk” Report, a study issued every two years to highlight programs that are “high-risk due to their greater vulnerabilities to fraud, waste, abuse, and mismanagement.”¹¹

In this year’s report, GAO warned that U.S. taxpayers are not receiving a “fair return” for oil and gas revenues under the terms of existing federal leases, and that correcting these deficiencies could save as much as \$53 billion. Specifically, GAO faulted so-called “royalty relief” granted by Congress in the mid-1990s to encourage additional exploration at a time when oil and natural gas prices were significantly lower. Under some of these leases, oil companies pay no royalties at all. According to GAO:

⁹ Staff Report, Senate Joint Economic Committee, *End Tax Breaks for Big Oil: Reduce the Federal Deficit Without Increasing Prices at the Pump* (May 2011) (online at jec.senate.gov/public/index.cfm?a=Files.Serve&File_id=def3390e-c933-4420-a076-19f786cd3af0) (internal footnotes omitted).

¹⁰ University of Massachusetts, Amherst and Political Economy Research Institute, *The Economic Benefits of Investing in Clean Energy*, at 28 (June 2009) (online at www.americanprogress.org/issues/2009/06/pdf/peri_report.pdf).

¹¹ Government Accountability Office, *High-Risk Series: An Update* (Feb. 2011) (GAO-11-278) (online at www.gao.gov/docsearch/featured/highrisk.html).

[S]pecial lower royalty rates—referred to as royalty relief—granted on leases issued in the deepwater areas of the Gulf of Mexico from 1996 to 2000—a period in which oil and gas prices and industry profits were much lower than they are today—could result in between \$21 billion and \$53 billion in lost revenue to the federal government, compared with what it would have received without these provisions.¹²

House Oversight Committee Chairman Darrell Issa has done significant work on this issue and has called for an end to these lease provisions. On October 7, 2009, he issued a staff report warning that actual shortfalls to U.S. taxpayers could be much higher. The report stated:

Depending upon the market price of oil and natural gas, the total cost of foregone royalties could total nearly \$80 billion. ... Oil and gas royalty payments represent one of the country's largest non-tax sources of revenue. Taxpayers must get every cent that is owed to them.¹³

At a hearing on March 3, 2011, Chairman Issa stated that “there is bipartisan support, still, to try to fix that.”¹⁴ To date, however, he and other Republican House Members have consistently voted against legislative efforts to correct this problem (see Section D, below).

D. Attempts to End Favorable Treatment for Oil Industry

Although House Republican leaders have repeatedly expressed support for ending tax subsidies, no-royalty leases, and other favorable treatment for the oil industry, every effort to pass legislation through the House has failed during this Congress.

On April 25, 2011, House Speaker John Boehner stated during an interview, “I don’t think the – the big oil companies need to have the oil depletion allowances.” He added:

We certainly oughta take a look at it. ... We’re in a time when – when the federal government is short on revenues. We need to control spending but we need to have revenues to keep the government movin’. And they oughta be payin’ their fair share.¹⁵

¹² Government Accountability Office, *High-Risk Series: An Update*, at 201 (Feb. 2011) (GAO-11-278) (online at www.gao.gov/docsearch/featured/highrisk.html).

¹³ Minority Staff Report, House Committee on Oversight and Government Reform, *Teapot Dome Revisited*, at 4, 8 (Oct. 7, 2009) (online at oversight.house.gov/images/stories/Reports/2009-10-07mmsreport.pdf).

¹⁴ House Committee on Oversight and Government Reform, *Hearing on Waste and Abuse: The Refuse of the Federal Spending Binge* (Mar. 3, 2011).

¹⁵ *Interview of House Speaker John Boehner*, ABC News (Apr. 25, 2011) (online at abcnews.go.com/Politics/transcript-abc-news-jonathan-karl-interviews-speaker-john/story?id=13455021).

Three days later, during a town hall meeting in Wisconsin on April 28, 2011, House Budget Committee Paul Ryan expressed support for ending tax subsidies for oil companies. His exchange with a constituent went as follows:

Question: The subsidy for the oil companies that the federal government gives. They've gotta stop.

Chairman Ryan: Sure.

Question: End the oil company subsidies...

Chairman Ryan: I agree.

Question: ...and you will gain a lot of that money in the red back.

Chairman Ryan: Right, so let me, one thing I didn't get into is, we're talking about reforming the safety net of the welfare system. We also want to get rid of corporate welfare. And corporate welfare goes to agribusiness companies, energy companies, financial services companies. So we propose to repeal all that.¹⁶

Despite these statements, every legislative effort to address these problems that has come before the House in the 112th Congress has failed. Some examples include the following:

- On February 18, 2011, House Republicans defeated, by a vote of 251 to 174, an amendment to H.R. 1 offered by Reps. Edward Markey, Maurice Hinchey, George Miller, and Lois Capps to recover up to \$53 billion from federal leases in the Gulf of Mexico that allow oil companies to drill without paying royalties.¹⁷
- On March 1, 2011, House Republicans defeated, by a vote of 249 to 176, a Motion to Recommit offered by Rep. William Keating to H.J. Res. 44 that would have repealed taxpayer-funded subsidies for oil companies.¹⁸
- On April 15, 2011, House Republicans passed, by a vote of 235 to 193, H. Con. Res. 34, the Fiscal Year 2012 budget resolution sponsored by Budget Committee Chairman Paul Ryan's, which retains approximately \$40 billion in tax subsidies and other favorable

¹⁶ *Paul Ryan Endorses Ending Oil Subsidies, Even Though He Voted for Them*, Wonk Room (Apr. 28, 2011) (online at wonkroom.thinkprogress.org/2011/04/28/ryan-oil-subsidies/#).

¹⁷ *Final Vote Results for Roll Call 109*, Clerk of the House (Feb. 18, 2011) (online at clerk.house.gov/evs/2011/roll109.xml).

¹⁸ *Final Vote Results for Roll Call 153*, Clerk of the House (Mar. 1, 2011) (online at clerk.house.gov/evs/2011/roll153.xml).

provisions for oil companies, while cutting investments in clean energy by approximately 70%.¹⁹

- On May 5, 2011, House Republicans defeated, by a vote of 241 to 171, a motion to consider Democratic legislation to prohibit the top five oil companies from receiving tax breaks for domestic manufacturing.²⁰
- On May 5, 2011, House Republicans defeated, by a vote of 238 to 171, a Motion to Recommit offered by Rep. Ben Ray Lujan to H.R. 1230 that would have required oil and gas produced under U.S. leases to be offered for sale only in the United States.²¹

¹⁹ *Final Vote Results for Roll Call 277*, Clerk of the House (Apr. 15, 2011) (online at clerk.house.gov/evs/2011/roll277.xml).

²⁰ *Final Vote Results for Roll Call 293*, Clerk of the House (May 5, 2011) (online at clerk.house.gov/evs/2011/roll293.xml).

²¹ *Final Vote Results for Roll Call 297*, Clerk of the House (May 5, 2011) (online at clerk.house.gov/evs/2011/roll297.xml).

II. COUNTERING SPECULATION WILL HAVE A DIRECT IMPACT ON PRICES AT THE PUMP

With gas prices now more than \$4 per gallon, industry officials, regulators, and outside experts have determined that prices are artificially high in part due to the actions of energy speculators. They believe excessive speculation could result in prices that are inflated by as much as 30%. Addressing excessive speculation offers the single most significant opportunity to reduce the price of gas for American consumers.

A. Experts Warn Against Manipulation by Speculators

In the futures market, where energy speculation typically takes place, legally binding futures agreements are bought and sold rather than the actual commodities themselves. These agreements are called futures contracts because they provide for the delivery of particular commodities during specified future timeframes. Commodities in a futures market may be bought or sold regardless of whether they are actually used or consumed by buyers or sellers.²²

Examples of futures exchanges include the Chicago Mercantile Exchange, the Chicago Board of Trade, the New York Mercantile Exchange, and the Intercontinental Exchange. The Commodity Futures Trading Commission (CFTC) is authorized to oversee the industry, and each of the U.S. futures exchanges operates as a self-regulatory organization, governing the conduct of its traders, brokers and the operation of the exchange.²³

Energy futures markets generally involve two types of traders—commercial hedgers and speculators. Hedgers are airlines, refineries, railroads, or other companies that depend on commodities for their underlying business. Hedgers trade in futures to offset risk; they attempt to lock in commodity prices today for transactions in the future.²⁴

In contrast, speculators seek to profit by forecasting price trends. Speculators do not typically have a consumption interest in the underlying commodities. Instead, they profit by predicting the future price of commodities. Speculators provide liquidity to the market by assuming the risks that hedgers wish to avoid. Of the two types of traders, speculators now represent the majority of participants in today's commodity futures markets.²⁵

²² Congressional Research Service, *Speculation and Energy Prices: Legislative Responses* (Aug. 6, 2008) (RL34555).

²³ Congressional Research Service, *Federal Financial Services Regulatory Consolidation: An Overview* (July 10, 2008) (RL33036).

²⁴ Congressional Research Service, *Speculation and Energy Prices: Legislative Responses* (Aug. 6, 2008) (RL34555).

²⁵ *Id.*

On May 12, 2011, Rex Tillerson, the CEO of ExxonMobil, testified before the Senate Finance Committee, along with the CEOs of five other major oil companies. During his testimony, he estimated that, without excessive speculation, oil would be trading at \$60 to \$70 a barrel instead of more than \$100 a barrel. Senator Maria Cantwell asked him, “What role do you think excessive speculation in the futures market is having on elevated oil prices?” In response, Mr. Tillerson initially said “it is very difficult to precisely say what impact it has.” They then had the following exchange:

Senator Cantwell: What do you think the price would be today if it was based on fundamentals of just supply and demand?

Mr. Tillerson: Well, again, it’s, if you were to use a pure economic approach, the economists would say it would be set at the price to develop the next marginal barrel.

Senator Cantwell: What do you think that would be today?

Mr. Tillerson: Well it’s pretty hard to judge but it would be, you know, when we look at it, it’s going to be somewhere in the \$60 to \$70 range.²⁶

On April 11, 2011, Goldman Sachs estimated that speculators may be inflating the price of oil by as much as \$27 a barrel, which could result in volatility. As a result, it warned clients to pull back on energy holdings and lock in existing profits. As reported by Reuters:

Long-term commodity bull Goldman Sachs warned clients on Monday to lock-in trading profits before oil and other markets reverse, with the bank’s estimates suggesting speculators are boosting crude prices as much as \$27 a barrel. ...

Using Goldman’s estimates, that indicates the total speculative premium in U.S. crude oil is currently between \$21.40 and \$26.75 a barrel, or about a fifth of the price.²⁷

On April 18, 2011, Michael Greenberger, a former CFTC Commissioner and authority on market regulation, testified before a House Agriculture Subcommittee that speculators have artificially increased demand and unmoored prices from market fundamentals. He stated:

[M]any company/commercial end-users, including, inter alia, Starbucks, Hershey, Lindt & Spruengli, and Delta Airlines, have now come forward demonstrating that the futures market is in complete disarray because of excessive speculation. The Commodity Markets Oversight Coalition, an independent, non-partisan and non-profit alliance of groups that represents commodity-dependent industries, businesses and end-users, has

²⁶ Senate Committee on Finance, *Hearing on Oil and Gas Tax Incentives and Rising Energy Prices* (May 12, 2011).

²⁷ *Goldman Spooks Oil Speculators with Call to Take Profit*, Reuters (Apr. 11, 2011) (online at ca.reuters.com/article/businessNews/idCATRE73A7YN20110411).

also adopted the position that commodity prices defy market fundamentals due to excessive speculation.²⁸

Writing for Forbes on May 13, 2011, Jason Raznick explained how high oil prices caused by excessive speculation may hamper the economic recovery:

Since the price of oil barrels is currently over \$100, it is clear that something beyond the laws of supply and demand is driving the high price of oil, and with it, the high price of gasoline. Well, if it isn't supply or demand that is driving the price of oil up so high, there's really only one other culprit: oil speculators. ... It is clear to any impartial observer that regulators need to clamp down in speculative trading in the oil market before the economy will ever fully recover.²⁹

B. The Influence of Speculators is Increasing Rapidly

Over the past decade, and particularly in the last several years, energy speculators have been rapidly replacing traditional commodity hedgers in the commodity futures trading markets.

On March 15, 2011, CFTC Commissioner Bart Chilton delivered the keynote address to a conference on Structured Trade and Finance in the Americas. He stated:

Economists at Oxford, Princeton, and Rice universities and many other private researchers say that speculators have had an impact on prices. ... There are now more speculative positions in commodity markets than ever before. Between June of 2008 and January 2011, futures equivalent contracts held by these types of speculators increased 64 percent in energy contracts. In June of 2008, the number of such contracts totaled 617,000. By September of 2010, they were 923,000. And, by January of this year, they had grown to 1,011,000.³⁰

²⁸ House Committee on Agriculture, Subcommittee on General Farm Commodities and Risk Management, Testimony of Michael Greenberger, *Hearing on Implementing Dodd-Frank: A Review of the CFTC's Rulemaking Process* (Apr. 13, 2011).

²⁹ *Even Oil Companies Know That Oil Prices Are Rigged*, Forbes (May 13, 2011) (online at blogs.forbes.com/benzingainsights/2011/05/13/even-oil-companies-know-that-oil-prices-are-rigged/).

³⁰ Commodity Futures Trading Commission, *Interconnectedness: Keynote Address of Commissioner Bart Chilton to the 13th Annual Structured Trade and Finance in the Americas Conference* (Mar. 15, 2011) (online at www.cftc.gov/PressRoom/SpeechesTestimony/opachilton-40.html).

More recently, on April 20, 2011, Commissioner Chilton stated: “There is a Wall Street premium on gas prices today. . . . Every time folks fill up their tanks, they can expect that several dollars are due to speculation.”³¹

Warnings about the growing influence of oil speculators began several years ago. In 2006, the Permanent Subcommittee on Investigations of the Senate Committee on Homeland Security and Governmental Affairs issued a report entitled, “The Role of Market Speculation in Rising Oil and Gas Prices.” The report found:

The large purchases of crude oil futures contracts by speculators have, in effect, created an additional demand for oil, driving up the price of oil to be delivered in the future in the same manner that additional demand for the immediate delivery of a physical barrel of oil drives up the price on the spot market.³²

The Senate report also explained how the increasing role of speculators caused upwards pressure on prices. It stated:

Although it is difficult to quantify the effect of speculation on prices, there is substantial evidence that the large amount of speculation in the current market has significantly increased prices. Several analysts have estimated that speculative purchases of oil futures have added as much as \$20–\$25 per barrel to the current price of crude oil, thereby pushing up the price of oil from \$50 to approximately \$70 per barrel. Additionally, by purchasing large numbers of futures contracts, and thereby pushing up futures prices to even higher levels than current prices, speculators have provided a financial incentive for oil companies to buy even more oil and place it in storage.³³

In 2008, the Subcommittee on Oversight and Investigations of the House Energy and Commerce Committee held hearings entitled, “Energy Speculation: Is Greater Regulation Necessary to Stop Price Manipulation?” One hearing witness, Fadel Gheit, Managing Director and Senior Oil Analyst at Oppenheimer & Co. Inc., testified that the increasing role of speculators was causing higher oil prices. He stated:

There were no unexpected changes in industry fundamentals in the last 12 months, when crude oil prices were below \$65 per barrel. I cannot think of any reason that explains the run-up in crude oil price, beside excessive speculation. . . . I do not believe the current record crude oil price is justified by market fundamentals of supply and demand. I

³¹ *Obama Blames Speculators for Rising Fuel Prices*, Reuters (Apr. 20, 2011) (online at www.reuters.com/article/2011/04/20/us-usa-energy-obama-speculators-idUSTRE73J1NN20110420).

³² Staff Report, Senate Committee on Homeland Security and Governmental Affairs, Permanent Subcommittee on Investigations, *The Role of Market Speculation in Rising Oil and Gas Prices: A Need to Put the Cop Back on the Beat* (June 27, 2006) (online at hsgac.senate.gov/public/_files/SenatePrint10965MarketSpecReportFINAL.pdf).

³³ *Id.*

believe the surge in crude oil price, which more than doubled in the last 12 months, was mainly due to excessive speculation and not due to an unexpected shift in market fundamentals.³⁴

C. Action to Counter Excessive Speculation

On July 21, 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act. The Act included several provisions intended to address excessive speculation, and the CFTC is in the process of developing regulations to implement these provisions.

Section 737 of the Dodd-Frank Act provided the CFTC with enhanced authority to establish and set position limits for speculators.³⁵ This provision was designed to “ban that speculation which exceeds the need for liquidity by commercial hedges in the commodity markets.”³⁶ Under this provision, Congress required the CFTC to implement aggregate position limits in energy commodities—including oil—within six months after enactment of the legislation. On January 26, 2011, the CFTC issued a proposed rule to begin the process of establishing position limits.³⁷

Section 736 of Dodd-Frank provided the CFTC with authority to raise margin limits for speculators who invest in commodities futures.³⁸ Margin limits are amounts that speculators purchasing oil futures must put aside as collateral for the exchange clearinghouse.³⁹ Currently, margin payments are set at roughly 6% of the total value of the contract. In contrast, the Federal Reserve Board, which determines initial margin requirements for securities trades, requires a

³⁴ House Committee on Energy and Commerce, Subcommittee on Oversight and Investigations, Testimony of Fadel Gheit, *Energy Speculation: Is Greater Regulation Necessary to Stop Price Manipulation? – Part II*, 110th Cong. (2008) (H. Rept. 110-128).

³⁵ Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203 (2010).

³⁶ House Committee on Agriculture, Subcommittee on General Farm Commodities and Risk Management, Testimony of Michael Greenberger, *Hearing on Implementing Dodd-Frank: A Review of the CFTC’s Rulemaking Process* (Apr. 13, 2011).

³⁷ Commodity Futures Trading Commission, *Position Limits for Derivatives*, 76 Fed. Reg. 4752 (Jan. 26, 2011).

³⁸ Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203 (2010).

³⁹ Center for American Progress, *Oil Roulette: Rising Oil Prices Harm American Families but Enrich Serial Speculators* (Apr. 28, 2011).

minimum margin payment of 50% of the purchase price.⁴⁰ When margin requirements were increased recently for silver futures, silver prices fell 27% in a single week.⁴¹

On April 21, 2011, President Obama directed Attorney General Eric Holder to create an Oil and Gas Price Fraud Working Group. The purpose of the group is to “monitor oil and gas markets for potential violations of criminal or civil laws to safeguard against unlawful consumer harm.”⁴² The group is a subset of the Financial Fraud Enforcement Task Force Working Group and includes representatives from the Department of Justice, the Commodity Futures Trading Commission, the Federal Trade Commission, the Department of the Treasury, and other federal agencies.

D. Support and Opposition for Solutions

On May 11, 2011, a bipartisan group of 17 Senators wrote to urge the CFTC to “take decisive action toward meeting its statutory deadline to implement new rules to protect consumers from excessive speculation and possibly manipulation in the energy futures and swaps markets.” The letter stated:

As record high volumes of financial oil speculation spike retail gasoline prices to levels unwarranted by supply and demand fundamentals, the CFTC has fallen dramatically behind in meeting the new Dodd-Frank statutory deadlines. ... [U]nder Dodd-Frank, Congress required—as opposed to merely authorized—the CFTC to implement aggregate position limits in energy commodities like oil within 180 days of the July 21, 2010 enactment date in order to “diminish, eliminate, or prevent excessive speculation.” ... The intent of this provision was to utilize the lessons learned from the oil price spikes of the summer of 2008 and prevent them from happening again.⁴³

Similarly, on May 16, 2011, 55 House Members sent a letter to Attorney General Eric Holder and the Chairman of the CFTC calling on both agencies to “exercise a variety of enforcement authorities to thoroughly investigate potential illegal activity in the oil futures market.” With respect to the CFTC, the letter stated:

The agency received new authority under last year’s Dodd-Frank financial reform legislation to limit excessive speculation and fix market failures in petroleum markets.

⁴⁰ Securities Exchange Commission, *Margin: Borrowing Money to Pay for Stocks* (Apr. 17, 2009) (online at www.sec.gov/investor/pubs/margin.htm).

⁴¹ *Response to Volatility in Silver Takes Hold*, New York Times (May 8, 2011) (online at www.nytimes.com/2011/05/09/business/economy/09commodities.html).

⁴² Department of Justice, *Attorney General Holder Announces Formation of Oil and Gas Price Fraud Working Group to Focus on Energy Markets* (Apr. 21, 2011) (online at www.justice.gov/opa/pr/2011/April/11-ag-500.html).

⁴³ Letter from 17 Senators to Commodity Futures Trading Commission (May 11, 2011) (online at <http://wyden.senate.gov/newsroom/press/release/?id=b3c5ea66-258c-4ebc-b6ec-61821d9fbe87>).

This authority includes the ability to establish speculative position limits and the authority to impose margin requirements to protect the financial integrity of the energy futures trading markets. The agency's efforts at implementing this authority are not proceeding fast enough—the CFTC should act swiftly to rein in dangerous activity in this market.⁴⁴

Rep. Walter Jones has also been outspoken on this issue. In addition to being one of three Republican House Members to vote against H.R. 1, he wrote on March 9, 2011, to “strongly urge” the CFTC to implement the provisions in the Dodd-Frank Act to counter excessive oil speculation. His letter stated:

[M]ost oil market experts agree that excessive, unnecessary speculation by Wall Street traders is part of the problem. ... Americans cannot wait until 2012; we need relief at the pump now! Further delay by the Commission leaves consumers and markets exposed to manipulation at a time when this nation can least afford it. It also threatens to derail any hope of economic recovery. On behalf of American people, I urge you to make this issue your top priority.⁴⁵

In contrast, when the Dodd-Frank Act passed in 2010, House Republicans voted almost unanimously against it.⁴⁶ On the day it passed the Senate, then-House Minority Leader John Boehner stated: “I think it ought to be repealed.”⁴⁷ After assuming control of the House in the 112th Congress, Republican leaders began taking several steps toward this goal:

- First, on January 5, 2011, Oversight Committee Chairman Darrell Issa joined seven other Members in introducing H.R. 87 to repeal the Dodd-Frank Act in its entirety.⁴⁸
- Second, on March 9, 2011, nearly all House Republicans voted in favor of H.R. 1, which would have cut the CFTC budget by nearly one-third.⁴⁹ CFTC Chairman Gary Gensler

⁴⁴ Letter from 55 Members of Congress to Attorney General Eric Holder and Commodities Futures Trading Commission Chairman Gary Gensler (May 16, 2011) (online at <http://braley.house.gov/images/stories/PDF/Oil.Speculation.Letter.Doj.CFTC.pdf>).

⁴⁵ Letter from Rep. Walter B. Jones to Commodity Futures Trading Commission (Mar. 9, 2011) (online at <http://jones.house.gov/News/DocumentSingle.aspx?DocumentID=228376>).

⁴⁶ H.R. 4173, Dodd-Frank Wall Street Reform and Consumer Protection Act (June 30, 2010) (House vote on conference report) (online at <http://thomas.gov/cgi-bin/bdquery/z?d111:HR04173:@@R>).

⁴⁷ *Senate Passes Wall Street Reform*, The Hill (July 15, 2010) (online at <http://thehill.com/homenews/senate/109053-senate-passes-wall-st-reform>).

⁴⁸ H.R. 87, To Repeal the Dodd-Frank Wall Street Reform and Consumer Protection Act (introduced Jan. 5, 2011) (online at <http://thomas.loc.gov/cgi-bin/bdquery/z?d112:HR00087:@@P/>).

stated that if these budget cuts were passed, “We’d have to have significant curtailment of our staff and resources. We would not be able to police ... or ensure transparent markets in futures or swaps.”⁵⁰

- Most recently, on May 18, 2011, Republicans on the House Agriculture Committee passed legislation that would delay the implementation of provisions in the Dodd-Frank Act, including regulations intended to counter excessive speculation in the oil futures market.⁵¹

These actions have been criticized by a variety of industry officials. For example, on March 31, 2011, Michael Fox, the Executive Director of Gasoline and Automotive Service Dealers of America, testified at a hearing before the House Committee on Natural Resources. He stated: “The fastest way to six dollar gasoline is to cut the funding to the CFTC.”⁵²

⁴⁹ H.R. 1, Full-Year Continuing Appropriations Act, 2011 (Mar. 9, 2011) (online at thomas.loc.gov/cgi-bin/bdquery/D?d112:1:./temp/~bdW1VJ:@@@R/home/LegislativeData.php).

⁵⁰ *Regulators: Wall Street Reform at Risk*, CNN (Mar. 1, 2011) (online at http://money.cnn.com/2011/03/01/news/economy/sec_cftc_funding/index.htm).

⁵¹ *House GOP Bill to Delay Financial Regulations Clears Key Hurdle*, Huffington Post (May 20, 2011) (online at www.huffingtonpost.com/2011/05/05/dodd-frank-repulican-financial-regulation_n_857917.html).

⁵² House Committee on Natural Resources, *Hearing on Harnessing American Resources to Create Jobs and Address Rising Gasoline Prices* (Mar. 31, 2011) (online at <http://naturalresources.house.gov/Calendar/EventSingle.aspx?EventID=228017>).

III. INCREASING DRILLING AND REPEALING SAFETY MEASURES WILL NOT LOWER GAS PRICES

In contrast to addressing excessive speculation, which may be inflating gas prices by up to 30%, experts believe that efforts to expand domestic drilling or eliminate safety measures put in place after the BP oil spill would have a negligible impact on gas prices, potentially saving only pennies per gallon even after several decades.

A. Additional Drilling Will Have Minimal Impact on Gas Prices

Government, industry, and outside experts have concluded that expanding domestic drilling would have a relatively insignificant effect on the price of gas for American consumers. Although expanding domestic drilling in a responsible and safe manner may offer other benefits, its effect on gas prices would be minor, according to experts.

The U.S. Energy Information Administration (EIA) is the nation's foremost independent source of energy information and analyses. In 2009, EIA examined the potential impact of expanding domestic oil exploration and drilling on the outer continental shelf of the Atlantic and Pacific coasts of the United States and the Eastern and Central regions of the Gulf of Mexico. EIA issued a report concluding that there would be no changes in gas prices by the year 2020, and that there would be a decrease of only 3 cents per gallon by the year 2030.⁵³

The primary reason for this result is that oil is a global commodity traded on the world market. On January 4, 2011, Ken Green, a resident scholar with the American Enterprise Institute, explained that new U.S. oil production would not affect the price of crude oil domestically. He stated: "The world price is the world price. Even if we were producing 100 percent of our oil, ... [w]e probably couldn't produce enough to affect the world price of oil."⁵⁴

Philip Verleger Jr., a prominent energy economist, agreed. He stated: "Suppose the U.S. were to boost production 1 million barrels a day. ... OPEC has the capacity to cut 1 million barrels."⁵⁵ Mr. Verleger also stated that the oil industry has successfully convinced the public of the false belief that there is a connection between U.S. drilling and oil prices.⁵⁶

⁵³ Energy Information Administration, *Impact of Limitations on Access to Oil and Natural Gas Resources in the Federal Outer Continental Shelf* (2009) (online at www.eia.gov/oiaf/aeo/otheranalysis/aeo_2009analysispapers/aongr.html).

⁵⁴ *As High Gas Prices Loom, New Congress Faces Pressure on Drilling*, New York Times (Jan. 4, 2011) (online at www.nytimes.com/gwire/2011/01/04/04greenwire-as-high-gas-prices-loom-new-congress-faces-pres-3445.html?pagewanted=2).

⁵⁵ *Id.*

⁵⁶ *Id.*

According to EIA, current U.S. field production of crude oil is at its highest level in almost a decade.⁵⁷ Some experts believe there is now a glut of oil on the market and that supply has overrun demand. On April 24, 2011, Rex Tillerson, CEO of ExxonMobil, stated that U.S. inventories are at “near record highs,” and “there is plenty of oil on the market.”⁵⁸

Despite this evidence, some proponents of drilling have blamed the Obama Administration for high gas prices. On April 20, 2011, for example, Oversight Committee Chairman Darrell Issa argued that the Administration’s policy toward offshore drilling “has resulted in higher prices for gas.”⁵⁹ Similarly, on May 6, 2011, former Alaska Governor Sarah Palin stated:

But rising gas prices—there is an inherent link, David, between energy and security, energy and prosperity, and energy and freedom, and this is something that obviously our president doesn’t understand because he’s doing all that he can to manipulate the U.S. supply of energy. He is diminishing and decreasing the amount of energy in our market domestically and that, of course, is resulting in prices that are rising and gas having doubled since he has been in office.⁶⁰

Numerous industry and other experts have repudiated these claims. For example, on March 10, 2011, Michael Canes, the former chief economist for the American Petroleum Institute, stated, “It’s not credible to blame the Obama Administration’s drilling policies for today’s high prices.” He also stated:

World oil prices are determined in a market of around 85 million barrels per day of production and consumption, while the consequences of domestic drilling, particularly in the Gulf, likely would be more in the range of several hundred thousand to one million barrels per day, and most of that production would not occur for a number of years.⁶¹

On March 14, 2011, Chris Lafakis, an economist at Moody’s Analytics, stated:

There is absolutely no merit to this viewpoint whatsoever. Near-term fluctuations in gasoline prices are determined by two primary factors: crude oil prices and seasonality.

⁵⁷ Energy Information Administration, *Domestic Oil Production Reversed Decades-long Decline in 2009 and 2010* (Apr. 27, 2011) (online at www.eia.doe.gov/oog/info/twip/twip.asp).

⁵⁸ *Oil Prices Reach Near Record Highs Despite Market Glut*, Arabnews.com (Apr. 24, 2011) (online at arabnews.com/economy/article371083.ece).

⁵⁹ Chairman Darrell E. Issa, *The Gulf Is Still Waiting for More Drilling Permits*, National Review Online (Apr. 20, 2011) (online at http://issa.house.gov/index.php?option=com_content&task=view&id=757&Itemid=92).

⁶⁰ *America’s Nightly Scoreboard*, Fox News (May 6, 2011) (online at <http://sarahpalininformation.wordpress.com/2011/05/06/18464/>).

⁶¹ *Energy Experts Reject Claim That U.S. Drilling Policies Caused Recent Jump In Gas Prices*, Media Matters (Mar. 14, 2011) (online at mediamatters.org/research/201103140030).

Since the deepwater drilling delay applies only to exploration and production, it would take years, maybe a decade to get any amount of crude oil out of the ground and into our gas tanks.⁶²

Similarly, Tom O'Donnell, a professor of Graduate International Affairs at The New School, stated:

The amount of extra oil that the U.S. would produce, as far as affecting the world price of oil, is almost insignificant. People who say producing more oil will bring price down for Americans are missing the fact that it's a world market. For instance, oil produced in North Slope may very well go to Japan. There's not a separate market—It's a world market.⁶³

B. Repealing Safety Measures Would Disregard Damage from BP Oil Spill

Despite claims from critics that safety measures put in place after the BP oil spill are harming local economies, they are designed to prevent a repeat of the massive economic and environmental devastation caused during and after the 87 days when oil gushed unabated into the Gulf of Mexico.

The explosions on the Deepwater Horizon drilling rig on April 20, 2010, killed 11 workers and resulted in the release of over 200 million gallons (4.9 million barrels) of oil into the Gulf of Mexico, creating the worst environmental disaster in the history of the United States. In January 2011, the National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling issued a report finding that oil from the Macondo well reached more than 780 miles along the Gulf, including salt marshes, mudflats, and sand beaches.⁶⁴

The BP oil spill devastated the fishing industry through closures—which at their peak amounted to nearly 37% of all federal waters in the Gulf—and through decreases in consumer demand for Gulf seafood.⁶⁵ According to market research commissioned by the Louisiana Seafood Promotion Board, “70% of consumers polled expressed some level of concern about seafood safety following the Gulf oil spill and 23% have reduced their consumption of seafood.”⁶⁶

⁶² *Energy Experts Reject Claim That U.S. Drilling Policies Caused Recent Jump In Gas Prices*, Media Matters (Mar. 14, 2011) (online at mediamatters.org/research/201103140030).

⁶³ *Id.*

⁶⁴ National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling, *Deep Water: The Gulf Oil Disaster and the Future of Offshore Drilling*, at 176 (Jan. 2011).

⁶⁵ *Id.* at 6.

⁶⁶ *Id.*

Other than Alaska, the Gulf Region produces the greatest amount of seafood by volume and value in the United States.⁶⁷ In 2008, Gulf commercial fishery landings totaled 1.27 billion pounds, with dock-side values of \$659 million.⁶⁸ In the same year, “the seafood industry of the Gulf States supported over 213,000 full- and part-time jobs with related income impacts of \$5.5 billion.”⁶⁹

The recreational fishing industry and associated businesses, such as bait and tackle shops, restaurants, hotels, and charters, also comprise a significant portion of the economy of the region. In 2008, 5.7 million visitors and residents took 24 million fishing trips spending more than \$12.5 billion on durable equipment and trips.⁷⁰

The presence of oil in coastal estuaries and wetlands along the Gulf coast “may alter migration patterns, decrease food availability, and disrupt life cycles.”⁷¹ Many species of commercial fish and shellfish begin early stages of development in coastal areas such as estuaries and wetlands before moving offshore and becoming adults.⁷² According to the National Oceanic and Atmospheric Administration (NOAA):

Ninety-seven percent (by weight) of the commercial fish and shellfish landings from the Gulf of Mexico are species that depend on estuaries and their wetlands at some point in their life cycle. Landings from the coastal zone in Louisiana alone make up nearly one-third (by weight) of the fish harvested in the entire continental United States.⁷³

According to recent reports, the Gulf experienced a 39% decline in commercial fish landings—representing a \$62 million loss in dockside sales.⁷⁴ NOAA reports that total commercial Gulf landings for shrimp species in 2010 decreased by 35.6 million pounds (27%) when compared to 2009.⁷⁵

⁶⁷ Congressional Research Service, *The Deepwater Horizon Oil Spill and the Gulf of Mexico Fishing Industry* (Feb. 17, 2011).

⁶⁸ National Oceanic and Atmospheric Administration, *NOAA’s Oil Spill Response: Fish Stocks in the Gulf of Mexico* (May 12, 2010).

⁶⁹ Congressional Research Service, *The Deepwater Horizon Oil Spill and the Gulf of Mexico Fishing Industry*, at 2 (Feb. 17, 2011).

⁷⁰ *Id.*

⁷¹ *Id.* at 7.

⁷² *Id.*

⁷³ National Oceanic and Atmospheric Administration, *Shorelines and Coastal Habitats in the Gulf of Mexico* (May 13, 2010).

⁷⁴ *The Gulf Coast One Year after the Deepwater Horizon Oil Spill*, PeterGreenberg.com (Apr. 19, 2011) (online at www.petergreenberg.com/b/The-Gulf-Coast-One-Year-After-The-Deepwater-Horizon-Oil-Spill/152605850798752191.html).

⁷⁵ Congressional Research Service, *The Deepwater Horizon Oil Spill and the Gulf of Mexico Fishing Industry*, at 5 (Feb. 17, 2011).

In addition to devastating the commercial and recreational fisheries industries, the BP oil spill decimated the Gulf's travel and tourism industries, which represent 46% of the Gulf's economy, generate over \$100 billion annually, and are responsible for over a million jobs.⁷⁶ The coastal communities of Mississippi, Alabama, and northwest Florida reported that combined lodging revenue dropped 12.9% for May through August 2010 compared to 2009—a loss of \$100 million for that peak summer period alone.⁷⁷ Some communities experienced more severe losses during those months with Gulf Shores and Orange Beach, Alabama, reporting a 41.5% drop in lodging revenue during those same months.⁷⁸

C. The “Permitiorium” is a Myth

Recently, critics have asserted that the Administration has instituted a “permitiorium,” or a de facto moratorium, on approving additional drilling permits in the Gulf. Although there is no evidence to support this claim, it appears to have been created by oil industry communications officials and repeated by Members of Congress. In fact, the Administration has approved multiple permits, and initial delays in obtaining permits were a result of the industry's ongoing efforts to develop an adequate technology to cap a blowout.

Jane Van Ryan is the Senior Communications Manager for the American Petroleum Institute. Over the past several months, she has stated on several occasions that the Obama Administration has put in place a “permitiorium,” or a ban on approving drilling permits in the Gulf. For example, on April 1, 2011, she stated: “The administration imposed a moratorium and a permitiorium on offshore drilling.”⁷⁹ In addition, on April 8, 2011, she stated:

[The] administration has a clear record of actions, including an offshore moratorium and permitiorium, that have reduced U.S. oil and natural gas development.⁸⁰

This exact rhetoric has been repeated by Oversight Committee Chairman Darrell Issa. For example, on April 20, 2011, he stated:

⁷⁶ *Oil Spill Damage Spreads through Gulf Economies*, CNNMoney.com (June 1, 2010) (online at money.cnn.com/2010/05/30/news/economy/gulf_economy/index.htm); *Update: Travel Industry Leaders Confront Gulf Crisis*, Travel Agent Central (June 21, 2010) (online at www.travelagentcentral.com/usa-southeast/update-travel-industry-leaders-confront-gulf-crisis-22078)

⁷⁷ *The Gulf Coast One Year after the Deepwater Horizon Oil Spill*, PeterGreenberg.com (Apr. 19, 2011) (online at www.petergreenberg.com/b/The-Gulf-Coast-One-Year-After-The-Deepwater-Horizon-Oil-Spill/152605850798752191.html).

⁷⁸ *Id.*

⁷⁹ *On Energy—Sitting Still*, Energy Tomorrow (Apr. 1, 2011) (online at blog.energytomorrow.org/2011/04/on-energy---sitting-still.html).

⁸⁰ *A Clean, Green Non Sequitor*, Energy Tomorrow (Apr. 8, 2011) (online at blog.energytomorrow.org/2011/04/a-clean-green-non-sequitur.html).

On the first anniversary of the Deepwater Horizon oil spill, the administration's de facto moratorium, or "permitorium," on offshore drilling has resulted in higher prices for gas.⁸¹

Similarly, on May 11, 2011, he stated:

As a direct result of President Obama's ban and subsequent "permitorium" against all drilling in the Gulf of Mexico, American production has dropped, and our country's energy needs have become increasingly dependent on foreign governments.⁸²

Contrary to these claims, no "permitorium" exists. The Administration has approved 14 deepwater drilling permits, 55 shallow water permits, and two new exploration plans.⁸³ All of these were approved after the lifting of a six-month moratorium established to allow industry officials time to develop new technologies to prevent and contain blowouts.

Soon after the initial explosions on the Deepwater Horizon, the President ordered the Department of Interior to determine whether "additional precautions and technologies should be required to improve the safety of oil and gas exploration and production operations on the outer continental shelf."⁸⁴ On May 27, 2010, the Department issued a report known as the "Safety Measures Report" which recommended several improvements, including enhancements for "blowout preventers."⁸⁵

Given the systemic and serious nature of problems identified in the Safety Measures Report, Interior Secretary Salazar issued a six-month moratorium on the drilling of deepwater wells in the Gulf of Mexico and Pacific Regions.⁸⁶ One of the primary reasons the Secretary

⁸¹ *The Gulf Is Still Waiting for More Drilling Permits*, National Review (Apr. 20, 2011) (online at issa.house.gov/index.php?option=com_content&view=article&id=757%3Athe-gulf-is-still-waiting-for-more-drilling-permits&catid=23%3Aopinion-editorials&Itemid=1).

⁸² Chairman Darrell E. Issa, *Issa Votes to End Obama's American Energy "Permitorium" in Favor of Lower Gas Prices and American Jobs* (May 11, 2011) (online at issa.house.gov/index.php?option=com_content&view=article&id=778:issa-votes-to-end-obamas-american-energy-permitorium-in-favor-of-lower-gas-prices-and-american-jobs&catid=63:2011-press-releases&Itemid=4).

⁸³ Bureau of Ocean Energy Management, Regulation and Enforcement, *Status of Drilling Permits & Plans Subject to Enhanced Safety and Environmental Requirements in the Gulf of Mexico* (online at www.gomr.boemre.gov/homepg/offshore/safety/well_permits.html) (accessed May 22, 2011).

⁸⁴ Department of the Interior, *Increased Safety Measures for Energy Development on the Outer Continental Shelf, Executive Summary* (May 27, 2010).

⁸⁵ *Id.*

⁸⁶ Minerals Management Service, *Notice to Lessees and Operators of Federal Oil and Gas Leases in the Outer Continental Shelf Regions of the Gulf of Mexico and the Pacific to*

ordered this suspension was that neither industry nor government possessed the technology to contain the Macondo well or respond adequately to the massive spill that resulted.⁸⁷ The absence of this technology allowed the Macondo well to flow unabated into the Gulf of Mexico for 87 days. The suspension was intended to allow time for oil companies to develop this technology.⁸⁸

Secretary Salazar formally lifted the suspension on October 12, 2010, acknowledging that there had been significant progress in addressing drilling safety, blowout containment, and spill response.⁸⁹ Prior to resuming drilling, however, operators would have to demonstrate their ability to deploy containment resources adequate to promptly contain a blowout in deepwater.⁹⁰

When the suspension was lifted, no operators had developed subsea containment technology to effectively contain a deepwater blowout.⁹¹ This changed on February 17, 2011, however, when the non-profit Marine Well Containment Company announced the completion of an initial response system that included a “subsea capping stack with the ability to shut in oil flow or to flow the oil via flexible pipes and risers to surface vessels.”⁹² Less than two weeks later, on February 28, 2011, the Administration approved the first of multiple deepwater drilling permits issued since the BP oil spill.⁹³

Implement the Directive to Impose a Moratorium on All Drilling of Deepwater Wells (May 30, 2010) (NTL no. 2010-N04).

⁸⁷ Secretary of the Interior, *Decision Memorandum Regarding the Suspension of Certain Offshore Permitting and Drilling Activities on the Outer Continental Shelf* (July 12, 2010).

⁸⁸ *Id.*

⁸⁹ Secretary of the Interior, *Decision Memorandum on Termination of the Suspension of Certain Offshore Permitting and Drilling Activities on the Outer Continental Shelf* (Oct. 12, 2010).

⁹⁰ Bureau of Ocean Energy Management, Regulation and Enforcement, *Statement of Compliance with Applicable Regulations and Evaluation of Information Demonstrating Adequate Spill Response and Well Containment Resources* (Nov. 8, 2010) (NTL No. 2010-N10).

⁹¹ Bureau of Ocean Energy Management, Regulation and Enforcement, *BOEMRE Director Discusses Future of Offshore Oil and Gas Development in the U.S. at Gulf Oil Spill Series* (Apr. 19, 2011) (online at www.boemre.gov/ooc/press/2011/press0419.htm).

⁹² *MWCC Announces Initial Deepwater Oil Spill Containment System*, eNewsUSA (Feb. 18, 2011) (online at enewsusa.blogspot.com/2011/02/mwcc-announces-initial-deepwater-oil.html).

⁹³ Bureau of Ocean Energy Management, Regulation and Enforcement, *BOEMRE Approves First Deepwater Drilling Permit to Meet Important New Safety Standards in the Gulf of Mexico* (Feb. 28, 2011) (online at www.boemre.gov/ooc/press/2011/press0228.htm).

D. Safety Measures Are Based on Lessons Learned from BP Oil Spill

In addition to requiring oil companies to develop and deploy technologies to prevent and contain deepwater blowouts, the Administration took several other steps to enhance the safety of drilling in the Gulf.

On May 22, 2010, the President announced the creation of the National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling, an “independent, nonpartisan entity” directed to “determine the causes of the disaster, and to improve the country’s ability to respond to spills, and to recommend reforms to make offshore energy production safer.”⁹⁴

After months of examination, the Commission issued a report in January 2011, concluding that the blowout of the Macondo well was preventable and occurred as a result of systemic failures by both industry and government.⁹⁵ The report stated:

In short, the safety risks had dramatically increased with the shift to the Gulf’s deepwaters, but Presidents, members of Congress, and agency leadership had become preoccupied for decades with the enormous revenues generated by such drilling rather than focused on ensuring its safety. With the benefit of hindsight, the only question had become not whether an accident would happen, but when. On April 20, 2010, that question was answered.⁹⁶

To address these problems, the Administration began by fundamentally reorganizing the Minerals Management Service (MMS), the component of the Department of Interior charged with overseeing drilling in the Gulf. MMS had been criticized previously because it was charged with overseeing the safety of drilling, the environmental impacts caused by drilling, and the revenue generated from drilling. According to the Commission report, MMS had a “built-in incentive to promote offshore drilling in sharp tension with its mandate to ensure safe drilling and environmental protection.”⁹⁷

On May 19, 2010, Secretary Salazar eliminated MMS and replaced it with the Bureau of Ocean Energy Management, Regulation and Enforcement (BOEMRE). Within BOEMRE, Secretary Salazar created three separate and independent bureaus:

- the Office of Natural Resources Revenue;
- the Bureau of Ocean Energy Management; and
- the Bureau of Safety and Environmental Enforcement.⁹⁸

⁹⁴ National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling, *Deep Water: The Gulf Oil Disaster and the Future of Offshore Drilling*, at vi (Jan. 2011).

⁹⁵ *Id.* at vii.

⁹⁶ *Id.* at 84-85.

⁹⁷ *Id.* at 56.

⁹⁸ Bureau of Ocean Energy Management, Regulation and Enforcement, *Fact Sheet: The BSEE and BOEM Separation* (Jan. 19, 2011).

On June 21, 2010, the Secretary swore in Michael R. Bromwich, the former Inspector General for the Department of Justice, as the new Director of BOEMRE.⁹⁹

Director Bromwich ordered the agency to conduct site-specific environmental assessments for all new and revised exploration and development plans.¹⁰⁰ This decision was based on the Commission’s finding that the practice of categorically excluding all exploration plans from review under the National Environmental Policy Act resulted in a systemic “breakdown of the environmental review process for OCS [outer continental shelf] activities.”¹⁰¹

BOEMRE established guidelines, through “notices to lessees,” that required operators to submit oil spill response plans that provide well-specific blowout and worst-case discharge estimates and to document the assumptions and calculations underlying those estimates.¹⁰²

BOEMRE also issued a Drilling Safety Rule to strengthen safety standards for well control procedures, drilling equipment (including blowout preventers), and well design, including both casing and cementing procedures. In addition, the Drilling Safety Rule required independent third-party inspection and certification of various capabilities of blowout preventers, including the ability to sever drill pipes under anticipated pressures.¹⁰³

BOEMRE also implemented a Workplace Safety Rule to require operators to put in place performance-based standards, similar to those used by regulators in the North Sea—where accident rates are much lower.¹⁰⁴

⁹⁹ Department of the Interior, *Salazar Swears-In Michael R. Bromwich to Lead Bureau of Ocean Energy Management, Regulation and Enforcement* (June 21, 2010).

¹⁰⁰ Bureau of Ocean Energy Management, Regulation and Enforcement, *BOEMRE Director Discusses Future of Offshore Oil and Gas Development in the U.S. at Gulf Oil Spill Series* (Apr. 19, 2011) (online at www.boemre.gov/ooc/press/2011/press0419.htm).

¹⁰¹ Senate Committee on Energy and Natural Resources, Testimony of Oil Spill Commission Co-Chairs Graham and Reilly, *Hearing to Review the Report and Recommendations, Including Any Recommendations for Legislative Action, Issued by the National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling*, at 12 (Jan. 26, 2011).

¹⁰² Bureau of Ocean Energy Management, Regulation and Enforcement, *Information Requirements for Exploration Plans, Development and Production Plans, and Development Operations and Coordination Documents on the OCS* (June 18, 2010) (NTL No. 2010-N06).

¹⁰³ Bureau of Ocean Energy Management, Regulation and Enforcement, *The Drilling Safety Rule: An Interim Final Rule to Enhance Safety Measures for Energy Development on the Outer Continental Shelf* (Sep. 30, 2010) (online at www.doi.gov/news/pressreleases/loader.cfm?csModule=security/getfile&PageID=45792).

¹⁰⁴ Deepwater Horizon Study Group, *Preventing Accidents in Offshore Oil and Gas Operations: The U.S. Approach and Some Contrasting Features of the Norwegian Approach*, at

Throughout this process, BOEMRE made significant efforts to conduct outreach and solicit feedback from industry stakeholders. Beginning in August 2010, BOEMRE launched a series of fact-finding forums in eight cities across the country to collect information and exchange views about deepwater drilling safety reforms, well containment, and oil spill response. BOEMRE also obtained input from 37 elected officials on the impact the oil spill had on their constituents.¹⁰⁵

In September 2010, BOEMRE obtained recommendations from two joint industry task forces regarding oil spill preparedness and response and subsea well control and containment, while a third industry task force made recommendations on May 17, 2010, relating to offshore drilling safety.¹⁰⁶ Task force participants included member companies and affiliates of the American Petroleum Institute, International Association of Drilling Contractors, Independent Petroleum Association of America, National Ocean Industries Association, and the U.S. Oil and Gas Association.¹⁰⁷ Many task force recommendations are reflected in the requirements issued by BOEMRE, including API standards governing the isolation of potential flow zones during well construction and safety management systems to identify, address, and manage operational safety hazards and impacts that are well-specific.¹⁰⁸

Most recently, in March 2011, BOEMRE held a workshop to assist industry officials with new safety requirements associated with new exploration and drilling permits.¹⁰⁹ The workshop was open to all Gulf of Mexico Region Outer Continental Shelf oil and gas stakeholders and was well-attended, with approximately 200 industry participants.

As a result of input from industry and a variety of other stakeholders, Secretary Salazar announced on May 14, 2011, that the Department of Interior would be implementing a number of actions to expand drilling in a safe and responsible manner. They include the following:

7 (Jan. 2011) (online at ccrm.berkeley.edu/pdfs_papers/DHSGWorkingPapersFeb16-2011/PreventingAccidents-in-OffshoreOil-and-GasOperations-MB_DHSG-Jan2011.pdf).

¹⁰⁵ Bureau of Ocean Energy Management, Regulation and Enforcement, *Public Forums on Offshore Drilling* (online at www.boemre.gov/forums) (accessed Mar. 28, 2011) (Sessions were held in New Orleans, Louisiana, on August 4, 2010; Mobile, Alabama, on August 10, 2010; Pensacola, Florida, on August 11, 2010; Santa Barbara, California, on August 24, 2010; Anchorage, Alaska, on August 26, 2010; Houston, Texas, on September 7, 2010; Biloxi, Mississippi, on September 10, 2010; and Lafayette, Louisiana, on September 13, 2010).

¹⁰⁶ Energy API, *Oil and Natural Gas Industry Calls for Offshore Safety Changes* (Sept. 7, 2010) (online at www.api.org/Newsroom/call-safety-changes.cfm).

¹⁰⁷ Joint Industry Oil Spill Preparedness and Response Task Force, *Draft Industry Recommendations to Improve Oil Spill Preparedness and Response* (Sept. 3, 2010).

¹⁰⁸ Joint Industry Task Force to Address Offshore Operating Procedures and Equipment, *White Paper: Recommendations for Improving Offshore Safety* (May 17, 2010).

¹⁰⁹ Bureau of Ocean Energy Management, Regulation and Enforcement, *BOEMRE to Hold Industry Workshop on Plan Processing* (Mar. 7, 2011) (online at www.boemre.gov/ooc/press/2011/press0307a.htm).

- (1) extending drilling leases in the Gulf and certain areas off the coast of Alaska;
- (2) incentivizing industry to develop unused leases both on and offshore;
- (3) conducting lease sales in Alaska's National Petroleum Reserve;
- (4) fast-tracking the evaluation of oil and gas resources in the mid- and south Atlantic Ocean;
- (5) holding Western and Central Gulf lease sales by mid-2012; and
- (6) establishing a high-level, cross-agency team to create a more efficient permitting process in Alaska to ensure that health, safety, and environmental standards are met.¹¹⁰

¹¹⁰ Senate Committee on Energy and Natural Resources, Testimony of Secretary of the Interior Ken Salazar, *Hearing to Hear Testimony on the Following Bills Related to Oil and Gas Development: S. 516, S. 843, S. 916, S. 917* (May 17, 2011).