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THE WHITE HOUSE

WASHINGTON

July 11, 1979

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MEMORANDUM FOR THE PRESIDENT

FROM: ALFRED E. KAHN *Fred*

SUBJECT: Short-Term Energy Policy

I emerged from our six hours of discussions at Camp David, Monday night and Tuesday morning, first impressed by the remarkable amount of unanimity on most counts, but second, with one major dissatisfaction: I felt we did not come to grips sufficiently with the urgent necessity of presenting to the American people a short-term strategy in the energy field that would convey to them a sense that we were assuming control over our energy destiny -- not by 1985 or 1990, but now.

The public is clearly most upset, at this very moment, about OPEC, gasoline supplies and prices. I fear that it will not be satisfied with another declaration of determination (such as it has already heard from Presidents Nixon and Ford) to press ahead with alternative long-term sources of supply that will reduce our dependence on imports by 1985 or 1990.

It was no accident, therefore, that Larry Klein and Ken Galbraith began their discussions at Camp David by proposing the adoption at once of the two cleanest alternative ways of closing the gap immediately -- decontrol of gasoline prices (Klein) and rationing (Galbraith). According to my notes, Marina Whitman, Bob Aboud and Reg Jones (who mentioned, additionally, the use of a big excise tax on gasoline as a means of getting the price up to market-clearing levels) supported the former, and Walter Heller and Governor Snelling the latter, with a couple of other people (like Steve Ross) supporting both.

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Both of these suggestions have enormous attractiveness. Imagine being able to declare to OPEC: beginning right now, we are going to decide how much of your oil we are willing to take; we are prepared to make whatever sacrifice is necessary to limit our bondage to you; for the rest of this year we are going to take an average of 7,500,000 b/d(say), no more; and we will find ways of living within that ration.

And yet I realize there are very strong reasons for not adopting either at this time, and I cannot quarrel with your rejection of immediate decontrol.

That poses a very painful dilemma, if I am right about what the American people will be looking for in your speech.

My suggestion is that you openly and honestly confront this dilemma, in the following ways:

1. You know that the American people are longing for a quick solution to the enormous problems created by our excessive dependence on OPEC and are anxious to fight back now.

2. Had the country begun what it should have begun five years ago, or what you urged it to do two years ago -- when you called for the moral equivalent of war, only to have that call ridiculed by cheap cynics and ignored by people of little vision -- we would be well on our way to a resolution today. Indeed, had we followed your lead, the price that OPEC would be in a position to extort from us today would probably be much lower than it is.

3. There are two possible immediate solutions, but it simply does not make sense to adopt them now: (a) decontrol would bring supply and demand into balance immediately by choking off demand to whatever extent is necessary -- after all, you do not see long waiting lines at our nation's beef counters -- but at possibly immense inflationary cost. No one can have any assurance that the price might not go up 35 or 50 cents; (b) the other solution would be comprehensive rationing. You will not shrink from that course when the occasion demands, but it simply does not make sense to impose this huge regulatory superstructure on the economy, at an estimated annual cost in the billions of dollars, in effect setting up a second currency to meet a supply shortfall on the order of maybe 5%.

4. What we can and must do, immediately, however, is institute a massive conservation and supply expansion strategy. This will begin to pay off right away, although it will take several years to make possible any real cut in imports. Second, we must immediately give you standby rationing authority, which you herewith declare your intention to invoke at once, in the event of any interruption of supply, or even a threatened interruption -- by Libya, Iran or anyone else; or any attempt by any country to use its oil to influence our foreign policy.

5. You are giving immediate effect to your Tokyo commitment to hold imports to 8,500,000 b/d by using authority you already have to impose a quota at that level.

I am not at all certain this kind of approach will suffice. But with decontrol of gasoline and gasoline rationing both ruled out at this time, I think such an approach would be better than ignoring the short-term urgencies entirely.

THE WHITE HOUSE
WASHINGTON

7-11-79

To Pat and Roy Marshall

Rosalynn and I share with you a deep feeling of both loss and sorrow. As you know, we loved Chris and admired his human qualities and his great courage.

We are available to help in any way possible, and will continue to carry you in our prayers.

Jimmy Carter

THE WHITE HOUSE
WASHINGTON

5/14/79

Mr. President:

The OMB summary decision memo includes all staff and agency comments.

Kahn, Lipshutz, Wexler and Rafshoon had no comment.

CL concurs with Eizenstat.

Bob Strauss' comments are attached.

Rick/Bill

THE WHITE HOUSE
WASHINGTON

July 11, 1979

MEMORANDUM TO THE PRESIDENT

FROM: STU EIZENSTAT *Stu*

SUBJECT: ATTACHED IMPORT REDUCTION DECISION MEMORANDUM

This memorandum is in response to your request for recommendations from the Energy Task Force on ways for the U.S. to reduce oil imports.

This is a lengthy memorandum on a very complex issue. I, therefore, recommend that you read the entire memorandum before making any decisions.

We will have a separate memorandum to you c.o.b. tomorrow on short term actions which could be taken to alleviate the current gasoline and distillate problem.

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IMPORT REDUCTION DECISION MEMORANDUM

I. INTRODUCTION

Recent events have underscored in an unprecedented way the unacceptable economic, national security and social risks inherent in high levels of U.S. oil imports.

Your advisors all agree that we must announce and implement a series of bold actions to reduce the Nation's dependence on OPEC oil, and that this endeavor needs to be credible, positive in tone, broad in scope, and stand as good a chance as possible of achieving its fundamental objective: a major reduction in oil imports. /

For these reasons, the Task Force has developed for your review three alternative import reduction levels, and different combinations of reduction measures to achieve those reduction targets.

The Congressional response to our recent energy difficulties has concentrated almost exclusively on a synthetic fuels production program. Producing synfuels, however, is not the only way to reduce oil imports. Because every marginal barrel of oil we consume is imported, every marginal barrel of oil we do not consume, as well as every additional barrel we produce, replaces a barrel of imported oil. Indeed, a combined program incorporating other initiatives, used in combination with synfuels programs of different sizes, will be more credible, cost less, be environmentally more benign, and be more likely to help achieve our import reduction objectives than a synfuels program alone. For those reasons, nearly all agencies recommend a broader program than synfuels alone--one that would reduce 1990 import levels by twice the target of the Moorhead Bill. ✓

The Task Force efforts were led by the Department of Energy and involved significant contributions by nearly a dozen agencies. Over the course of the last several weeks, the Task Force undertook an examination of three broad approaches to reducing oil imports:

- o synthetic fuels production
- o increased domestic production of unconventional oil and gas
- o conservation and fuel switching

In addition, the Task Force reviewed alternative organizational options, particularly the government corporation approach, as well as different means of accomplishing "fast-track" permitting of critical new energy facilities. From the results of this work, the Task Force developed several programs for the investment of the billions of dollars collected by the Windfall Profits Tax.

This decision memorandum is structured in a way that mirrors the analytic approach used by the Task Force. Section III provides you with a overview of the major import reduction options considered. Section IV describes these measures in greater detail and outlines the costs per barrel of oil saved, the appropriate institutional and financing devices for each measure, and their relationship to the organization and "fast-track" issues.

Section V reviews the organizational options. Section VI examines the "fast-track" alternatives. Section VII discusses the potential use of import quotas in addition to or instead of goals or targets.

Section II, the background section:

- o Sets out the future world oil price assumptions used by the Task Force.
- o Reviews the "base case" of this analysis.
- o Summarizes the three alternative import reduction target levels for 1990.
- o Provides a "balance sheet" for the Energy Security Trust Fund.
- o Discusses the uncertainty that necessarily affects all dimensions of this analysis and, therefore, the policy choices you are asked to make.

II. BACKGROUND

A. Future World Oil Prices

Table 1 shows the world oil price assumptions used in the Task Force analysis. The Low and Medium price cases are virtually the same as the old Medium and High cases, respectively, that predated the June OPEC price hikes. The High price case in Table 1 is a new case developed for the Task Force analysis.

TABLE 1

WORLD OIL PRICE ASSUMPTIONS: 1980-2000
(1979 \$/barrel)

<u>Price Case</u>	<u>1980</u> ^{1/}	<u>1985</u>	<u>1990</u>	<u>1995</u>	<u>2000</u>
<u>Low</u> (1.4% annual real growth 1980-90)	20	20	23	27	32
<u>Medium</u> (3.2% annual real growth 1980-90)	22	25	30	38	42
<u>High</u> (4.8% annual real growth 1979-90)	25	31	37	42	48

The Medium price case was used to generate the estimated costs per barrel, budget costs and investment requirements set forth throughout this memorandum. In our judgment, the Medium price case lies at the high end of the most plausible projections of OPEC behavior over the period 1980-90. However supply interruptions or other cartel actions may well drive the price substantially above this trend line for periods of time within this period. The Medium case assumes that although the OPEC nations have learned in recent months that they can charge increasing prices for lower total oil production without substantially reducing current cash flow, they nevertheless will be constrained by a twin reluctance to ruin the LDC's and to cripple the economy of the industrialized nations.

The Low price case, although supported by pre-1978 pricing history, appears overly optimistic in suggesting that the OPEC nations would ignore their 1978-79 experience in future years.

^{1/} The June 1979 OPEC decision raised U.S. import prices to about \$22 average per barrel (refiner acquisition cost).

*Must avoid
condoning or
expecting OPEC
price rises*

The High price case, on the other hand, would imply a willingness on the part of the OPEC nations to threaten destruction of the world economy with cumulative price shocks resulting in a 1990 price of \$70 per barrel in 1990 dollars.

Generally speaking, the higher the path one believes world oil prices will follow, the more attractive become the more expensive import reduction investments (e.g., synthetic coal liquids), and the lower the budget cost of supporting those investments through guaranteed purchases or other subsidies.

B. The Base Case

The current base case projection of 8.0-8.5 MMB/D for 1990 oil imports also are based on the Medium world oil price case. In addition, the base case includes the effects of Administration actions to date, such as the NEA, oil decontrol, and the recently announced solar initiatives. The components will be broken out for presentation.

C. Optional Import Reduction Levels

Oil import levels in 1990 obviously will be subject to a wide range of uncertainties. The Task Force developed and examined four broad options to reduce oil imports from base case levels. As Table 2 shows, these would reduce imports from our otherwise projected levels of 8.0-8.5MMB/D by a total of 3, 4, or 5 MMB/D by 1990, using combinations of measures to produce synthetic fuels, to encourage and finance conservation and fuel switching investments, and to stimulate production of oil and gas from non-conventional sources.

TABLE 2

IMPORT REDUCTION OPTIONS
(millions of barrels per day)

1990

<u>Program Component</u>	<u>Option</u>			
	<u>A</u>	<u>B</u>	<u>C</u>	<u>D</u>
Synthetic Fuels ^{1/}	0.5	1.0	2.0	2.0
Conservation, Fuel Switching, Uncon- ventional Oil and Gas	2.5	3.25	2.0	3.25
Total	3.0	4.25	4.0	5.25

Table 3 displays the composition of the options in more detail, along with cost per barrel and budget cost estimates. For general comparisons, the Moorhead Bill establishes a goal of 2 million barrels per day of synfuels production -- including heavy crude oil -- by 1990; heavy crude production at a 500,000 barrels per day level is included in Options A-D as a non-synthetic fuel.

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^{1/} Includes oil shale, coal liquids, coal gasification and biomass conversion. Does not include heavy crude oil production, because technically it is not a synthetic fuel. (The Moorhead Bill includes .5MMB/D in heavy oil within its goal of 2 MMB/D of synthetic fuels.)

TABLE 3 - IMPORT REDUCTION OPTIONS

Average Cost
Per Barrel

A. 3 MMB/D

Source	syn-fuels	heavy oil	unconven. gas	utility oil	R/C retro.
Price (\$/bbl.)	\$40	\$28	\$26	\$25	\$5-\$10
Budget (billions)	\$8	--	\$1.0	\$3.8	\$1.5

*\$40/b too high?
Cumulative budget?
- 10%/yr > '85*

\$25

Nuclear?

Expedited leasing

B. 4 MMB/D

Source	synfuels	heavy oil	unconven. gas	utility oil	R/C retro	Auto/transit
Price (\$/bbl.)	\$40	\$28	\$26	\$27	\$10	\$15 --
Budget (billions)	\$27	--	\$1.0	\$5.0	\$1.5	6.4 \$10

\$27

C. 4 MMB/D

Source	synfuels	heavy oil	unconven. gas	utility
Price (\$/bbl.)	\$40	\$28	\$26	\$27
Budget (billions)	\$63	--	\$1.0	\$3.75

\$32

D. 5 MMB/D

Source	synfuels	heavy oil	unconven. gas	utility oil	R/C retro	Auto/transit
Price	\$40	\$28	\$26	\$25	\$5-\$10	\$15 --
Budget (billions)	\$63	--	\$1.0	\$5.0	\$1.5	6.4 \$10

\$30

D. Energy Security Trust Fund

Tables 4-A, B and C show the relationship between the Energy Security Trust Fund revenues and the budget costs of the alternative import reduction strategies. Table 4-A assumes the Low world oil price path, Table 4-B the Medium path, and Table 4-C the High path.

Several points deserve emphasis in connection with these Tables:

- o The eventual size of the Trust Fund is as uncertain as the oil price path; it depends entirely on the final scope, bite and duration of the windfall profits tax. We believe \$140 billion for 1980-90 to be a generous, optimistic estimate, since the Senate is likely, in our judgment, to pass a significantly more lenient bill than the House.^{1/}
- o The actual oil price path will affect both the size of the Trust Fund and the total budget cost of the various import reduction measures.
- o The budget costs shown in these Tables do not by any means reflect the total costs to the economy of making the investments in import reductions. These represent only the share of the total cost borne by the Federal government.
- o The most significant variance in Federal budget costs is between Options B (low synthetics) and C (high synthetics) at Low and Medium world oil prices. Although both strategies can generate overall import reductions of 4 MMB/D, the \$40 per barrel price required to bring on line many of the coal synthetics will bite very hard if world oil prices are low.

^{1/} The estimated revenues are based on the assumptions that the Administration proposal is enacted and that the Medium oil price path prevails.

TABLE 4 A ENERGY SECURITY TRUST FUND¹

Budget Balances	IMPORT REDUCTION OPTIONS - LOW PATH			
	A - 3 MMB/D	B - 4 MMB/D	C - 4 MMB/D	D - 5 MMB/D
o Estimated Budget Expenditures for Import Reduction Option ²	\$64	\$165	\$311	\$321
o Estimated Trust Fund Revenues (after April 5 commitments) ³	\$107	\$107	\$107	\$107
o Net Balance of Trust Fund (after Import Reduction Option) ⁴	\$43	\$(58)	\$(202)	\$(214)

1. All dollars are estimated in nominal terms using the July budget update inflation assumptions.
2. Assumes low oil price case of \$22 in 1985 and \$23 in 1990 in real terms.
3. Revenues are for 1980-90 based on the Administration proposal less the cost of the April 5 Message initiatives (excluding shale oil) and the Solar Bank.
4. Net balance of the Trust Fund after expenditures. () indicate negative balance or a requirement for funding from the President's budget.

NOTE: This is an extremely optimistic view which was not used for purposes of the computations made by the inter-agency task force

TABLE 4 B ENERGY SECURITY TRUST FUND¹

Budget Balances	IMPORT REDUCTION OPTIONS - MIDDLE PATH			
	A - 3MMB/D	B - 4MMB/D	C - 4 MMB/D	D - 5 MMB/D
o Estimated Budget Expenditures for Import Reduction Option ²	\$ 17	\$ 45	\$ 71	\$ 80
o Estimated Trust Fund Revenues (after April 5 commitments) ³	\$107	\$107	\$107	\$107
o Net Balance of Trust Fund (after Import Reduction Option) ⁴	\$ 90	\$ 62	\$ 36	\$ 27

1. All dollars are estimated in nominal terms using the July budget update inflation assumptions.
2. Assumes medium oil price case of \$25 in 1985 and \$30 in 1990 in real terms.
3. Revenues are for 1980-90 based on the Administration proposal less the cost of the April 5 Message initiatives (excluding shale oil) and the Solar Bank.
4. Net balance of the Trust Fund after expenditures. () indicate negative balance or a requirement for funding from the President's budget.

TABLE 4 C ENERGY SECURITY TRUST FUND ¹

Budget Balances	IMPORT REDUCTION OPTIONS- HIGH PATH			
	A - 3 MMB/D	B - 4 MMB/D	C - 4 MMB/D	D - 5 MMB/D
o Estimated Budget Expenditures for Import Reduction Options ²	\$11	\$25	\$26	\$35
o Estimated Trust Fund Revenues (after April 5 commitments) ³	\$107	\$107	\$107	\$107
o Net Balance of Trust Fund (after import reduction Options) ⁴	\$96	\$82	\$81	\$72

1. All dollars are estimated in nominal terms using the July budget update inflation assumptions.
2. Assumes high oil price case of \$25 in 1985 and \$30 in 1990 in real terms.
3. Revenues are for 1980-90 based on the Administration proposal less the cost of the April 5 Message initiatives (excluding shale oil) and the Solar Bank.
4. Net balance of the Trust Fund after expenditures. () indicate negative balance or a requirement for funding from the President's budget.

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*Long will cut back
w/ fall tax to eliminate
Trust fund balance*

The magnitudes of the trade and security effects are harder to quantify but, unlike the oil price effects, the security effects cannot be offset by OPEC production responses.

2. Results of Import Reduction Measures in Barrels per Day

The numerical estimates of barrels per day saved or replaced by all of the measures are very rough, with margins of error in the hundreds of thousands of barrels.

The estimates for the synthetics production measures are uncertain on account of both the environmental and technological unknowns and the need for private sector response. To assume that the synfuels corporation will meet its target exactly (whatever level is selected) is probably optimistic. On the other hand, under the assumptions DOE has used, the savings and production estimates for the conservation, fuel switching and unconventional gas and oil production measures are probably ^{As a whole,} therefore, we believe that the overall estimates for the Options are reasonable.

3. Costs of the Measures

We have noted before that the cost estimates are highly sensitive to the world price of oil. The costs versus savings impacts of deviations from the Medium world oil price cases on the two broad categories of import reduction measures, can be further illustrated by Table 5.

Because the synthetic programs hold production levels constant regardless of world oil price paths, world oil price variations only affect government costs. In the conservation, fuel switching and other oil and gas production programs, on the other hand, price path variations impact both government costs and import savings.

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*Alkins says OPEC
top price
will match
collective
cost of synfuels*

? understated.

- o The Trust Fund will be the sole source of funds for the expenditures proposed in the Options. To the extent that the Windfall Profits Tax fails to provide adequate revenues, downward adjustments in these programs will have to be made. Otherwise, new burdens will be placed on what likely will be a strained base Federal budget.

E. Uncertainties and Risks

We want to emphasize the high degree of uncertainty which runs through this entire analysis. Substantial margins of error necessarily accompany the estimates given the nature of the variables we are dealing with. You should treat these estimates and our conclusions cautiously. Some of the reasons for that caution are discussed in this Section.

1. The Benefits of Import Reduction

There would be some, though unquantifiable costs, to the nation to domestic and international security if we fail to reduce imports. Reducing imports also can yield quantifiable benefits to the economy beyond the savings calculated on a per-barrel basis as a result of the following effects:

- o Price - pressure on world oil markets will be reduced, possibly resulting in lower prices paid for remaining U.S. imports (if OPEC production is not cut to match U.S. import reductions);
- o Trade - reduced and possibly cheaper oil imports will improve the balance of trade, strengthen the dollar and reduce the cost of oil imports as well as inflationary pressures;
- o Security - lower imports will reduce economic and strategic vulnerability, while providing greater flexibility in foreign policy.

Calculations of these values of reduced demand for OPEC oil through import reductions indicate economic savings range from \$2 to \$5 per barrel, with lower values being more probable. The magnitude of these savings is uncertain because the most important component of the savings is the price effect; if OPEC cuts production to match U.S. import reductions, or if other nations increase imports by the same amount, those savings could vanish.

*OPEC wants to cut
(some nations must cut)*

*They probably →
won't - we'll keep
pressure on.*

III. Description of the Overall Import Reduction Options

Four broad options to reduce projected 1990 imports by three target levels -- 3 MMB/D, 4 MMB/D, and 5 MMB/D -- are presented for your consideration. Assuming 1990 imports are 8.5 MMB/D under the Base Case, these options would reduce 1990 import levels to 6.5, 5.5, and 4.5 MMB/D respectively. 77

The basic strategies used to achieve these reductions range from a modest synthetics/medium conservation approach to a very heavy synthetics option. This section highlights the major elements of the options, the differences between them, and agency recommendations. Clearly, any number of other options could be formulated using different combinations of these measures.

OPTION A: 3 MMB/D Reduction Using Modest Synthetics and Medium Conservation Tools.

Under this approach savings would be achieved by:

Synthetic fuels	500 (B/D)
Unconventional Gas	750
Heavy Oil	500
Residential/Commercial Retrofit	500
Utility Oil Back-out	<u>750</u>
TOTAL	3000

Cost to USG: \$17 Billion (nominal \$)

This is the least costly option, both in budget terms and cost per barrel saved. It is the most easily achievable target, and would require the fewest changes in existing organizational structures, regulatory requirements, or current program direction.

None of your advisors are recommending this approach, though some feel that the synfuels level contained in it is the most realistic of the four. All recognize that this program is too modest given the need for a "call to arms" on energy.

OPTION B: 4 MMB/D Reduction Using Strong Synthetics,
Strong Fuel Switching and Strong Conservation

1990 savings would be achieved by:

Synthetic Fuels	1000-1,500 (B/D)
Unconventional Gas	750
Heavy Oil	500
Improved Auto Fleet Efficiency	250
Residential/Commercial Retrofit	500
Utility Oil Back-out	<u>1000</u>
TOTAL	4000

Cost to USG: \$45 Billion (nominal \$)

This option provides a strong production program divided among synthetics, unconventional oil, gas and coal use. It also contains strong, new conservation initiatives. It is designed to commit to 1 MMB/D synthetics, with a possible increase to 1.5 MMB/D, if the Corporation established to implement this program finds, after review, that this can be accomplished. If heavy oils are included in the definition of synthetics, as the Moorhead bill does, this program could be presented as achieving 1.5 MMB/D synthetics, with an option to go to 2 MMB/D should that prove feasible. This option contemplates establishment of a corporation for synthetics, and substantial streamlining of regulatory requirements through an Energy Mobilization Board.

OMB, DPS, Kahn, NSC and Treasury recommend this approach because it makes a firm commitment to synthetics without overstating what those agencies now believe is feasible, and it also provides strong initiatives in conservation, fuel switching and unconventional oil and gas which could have good pay off in 1985 as well as 1990. These agencies believe that the option for the Corporation to submit plans, if feasible, for an additional 500 MMB/D is essential to prevent adverse Congressional reaction and that the opportunity to pursue such additional capacity, if it is feasible, is substantively important.

While recognizing that the political climate requires you to set a national production goal for substitute fuels, CEQ, EPA and Interior believe that the goal should not exceed 1 million b/d of synfuels by 1990, and that it should be qualified by a clear recognition of the economic and

environmental risks. They therefore do not support allowing the Corporation to recommend adding up to .5 million b/d to the 1990 goal. They have serious doubts about committing ourselves now to a large synfuels industry instead of other import reduction programs. Reliance upon synthetic fuels would be both environmentally injurious and extremely expensive -- involving as it does mammoth capital outlays and heavy demand for additional transport facilities and scarce labor skills. Environmentally, the CO2 problem in particular suggests caution.

These agencies believe there are alternative ways of reducing oil imports, including conservation and production of unconventional natural gas and heavy oil, that may prove to be quicker, cheaper and cleaner -- and that any greater commitment to synfuels should await further experience.

OPTION C: 4 MMB/D Using Strongest Synthetics, Strong Production, and Fuel Switching

1990 savings would be reached by:

Synthetic Fuels	2000
Unconventional Gas	750
Heavy Oil	500
Utility Oil BackOut	<u>750</u>
TOTAL	4000

Cost to USG: \$70 billion (nominal \$)

This option increases synthetics production targets by 1 MMB/D above Option B, and contains no conservation initiatives. It reflects DOE's opinion that synthetic fuels investments are more likely to work than regulatory conservation efforts, that synfuels investments are more likely to be enacted by Congress than regulatory initiatives, and in addition that a program with an exclusive focus on production is more attractive politically than the alternatives presented. It includes a corporation to manage the synthetics program, and an Energy Mobilization Board to streamline the regulatory process.

It is recommended by the Department of Energy because it is almost exclusively production oriented and makes a strong commitment to streamlined procedures through an Energy Mobilization Board and a new corporation within the Department of Energy. To provide balance, DOE also recommends that conservation initiatives along the lines of Option B should be proposed. — >

OPTION D: 5 MMB/D Using Strongest Synthetics, and
Maximum Savings from Other Sources.

1990 savings would be achieved by:

Synthetic Fuels	2000
Heavy Oil	500
Unconventional Gas	750
Auto Efficiency	250
Utility Oil Back-out	1000
Residential/Commercial Retrofit	<u>500</u>
TOTAL	5000

Cost to USG: \$80 billion (nominal \$)

This approach relies very heavily on synthetics, as well as strong approaches to reductions from unconventional oil and gas, utility oil back-out, and conservation. Its total savings go well beyond any current Congressional proposal, and would rely very heavily on streamlining of regulatory processes, heavy Federal spending, and establishment of a new Corporation, whether inside or outside DOE.

It is not recommended in full by any of your advisors.

The following table shows a more detailed breakdown of the four options.

TABLE

OIL IMPORT REDUCTION OPTIONS

		<u>OPTION A</u> <u>3 MMBPD Total</u>	<u>OPTION B</u> <u>4 MMBPD Total</u>	<u>OPTION C</u> <u>4 MMBPD Total</u>	<u>OPTION D</u> <u>5 MMBPD Total</u>
SOURCES: (Amounts in MMBD in 1990)					
<u>SYNFUELS</u>	<u>Subtotal</u>	<u>(0.5)</u>	<u>(1.0)</u>	<u>(2.0)</u>	<u>(2.0)</u>
SHALE OIL		0.25	0.25 ← low	0.4	0.4
COAL SYNTHETICS		0.22	0.70 ← low	1.5	1.5
(Indirect Liquefaction)		(0.07)	(0.40)	(1.0)	(same as Option C)
(Direct/Catalytic liquefaction)		(0.10)	(0.15)	(0.3)	
(Coal gas: high or medium)		(0.05)	(0.15)	(0.2)	
BOIMASS		0.05	0.05	0.1	0.1
<u>UNCONVENTIONAL OIL & GAS</u>	<u>Subtotal</u>	<u>(1.25)</u>	<u>(1.25)</u>	<u>(1.25)</u>	<u>(1.25)</u>
HEAVY OIL		0.5	0.5	0.50	0.5
UNCONVENTIONAL GAS	0.75	0.75	0.75	0.75	0.75
<u>CONSERVATION AND FUEL SWITCHING</u>	<u>Subtotal</u>	<u>(1.25)</u>	<u>(1.75)</u>	<u>(0.75)</u>	<u>(1.75)</u>
UTILITY OIL BACKOUT REQUIREMENT		0.75	1.0	.75	1.0
RESIDENTIAL/COMMERCIAL RETROFIT FINANCING		0.5	0.5	← ?	0.5
AUTOMOTIVE EFFICIENCY IMPROVEMENTS		---	0.25	--- ← ?	0.25
<u>TOTAL BUDGET COSTS</u>		<u>\$17</u>	<u>\$45</u>	<u>\$70</u>	<u>\$80</u>
(in billions)					

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IV. TOOLS AVAILABLE FOR IMPORT REDUCTIONS

This section of the memorandum describes the specific import reduction tools available for conservation and fuel switching, synthetics, and unconventional oil and gas. The potential import reductions, budget impacts, the estimated per barrel cost and analysis of each of these mechanisms are set out below.

A. Conservation and Fuel Switching Initiatives

1. Residential Conservation

In addition to the tax credits and other conservation programs contained in the National Energy Act, there are significant savings potentials with an accelerated residential conservation program. These initiatives are:

o A mandatory requirement that gas and electric utilities provide to all homeowner or apartment owner customers (who use these fuels for space heating) financing for conservation in the form of a long-term loan. Conversion from oil to gas heat would also be eligible for financing by gas utilities under this initiative. The cost of this financing would be included in the utility rate base, thereby spreading the costs of the loan across all the utility's customers.

The consumer would incur no additional costs beyond his normal monthly utility bill until the home (or apartment building) was sold. At time of sale, the full principal amount of the loan would have to be repaid. Other ratepayers would receive benefits since conservation investments are cheaper than constructing new generating capacity. A voluntary financing program using this system has operated in Oregon for about one year with good success.

Estimated savings: 250,000 barrels per day. Potential savings range up to 500,000 B/D.

Budget impact: Zero since utilities would bear all the costs of financing the loans.

Estimated cost per barrel: \$5-\$10.

o For oil-heated homes (which cannot take advantage of the utility financing program for gas or electric heat) an interest subsidy for conservation and retrofit loans would be provided by the government. Apartment building owners would also be eligible for this loan program, with a requirement that savings be passed through to apartment renters or individual owners. ✓

utility financing doubtful - motivation?

Estimated savings: 250,000 B/D.
Potential savings up to 500,000 B/D.

Budget impacts: \$150 million per year for ten years to cover subsidies and defaults.

Cost per barrel saved: \$5 to \$10.

Discussion

Utility financing of conservation improvements was recommended in your April 1977 program. Congress rejected, and expressly prohibited, however, utility involvement in conservation financing because of consumer antagonism toward utilities, fears that utilities would monopolize the conservation/retrofit business, and utility opposition to the program. Whether the urgency of the current situation has changed that view is unknown. In any event, enactment of such a program will require a strong Administration push.

Because utilities have access to capital at lower than market rates, can provide long-term financing, and are regulated, this approach remains, at least for gas and electric heated homes, a strong means of accelerating conservation investments at very low per barrel costs.

Utility financing for oil-heated homes was not recommended because neither gas nor electric utilities will benefit in terms of future capacity requirement reductions by improving efficiency in those homes. A major equity problem arises if gas and electric heating customers are asked to subsidize (through inclusion of oil-heated conservation in their rate base) investments which would not benefit them or the longer term needs of their utility.

2. Transportation Efficiency

For the period 1980-90 the following funds have been earmarked for transportation as follows:

	(Total)	(Annual)
Improvements to Existing Mass Transit Systems	\$11 billion	\$1.0
Improved auto Efficiency	<u>6.4 billion</u>	<u>.6</u>
Total	\$17.4 billion	1.6

Discussion

Secretary Adams has proposed these investments and suggested that they will permit savings at well over 500,000 B/D of oil by 1990 (current consumption in the transportation sector is 8 MMB/D). The Task Force supports the Secretary's recommendation. However, because DOT has not yet developed specific proposals we suggest allocating the funds and approving the targets for reduction of consumption, and that you direct DOT to return to you with their specific proposals within two weeks.

3. Conversion of Oil-Fired Utility Boilers

This initiative would seek legislation to require that utilities reduce current oil usage by a specified percentage (50% or 65%) by 1990. Incentives would be provided to encourage utilities to invest in new non-oil generators, thereby retiring oil-fired plants before the end of their useful lives. This proposal covers oil-burning plants which once were coal-capable as well as those which were and are not coal-capable.

The initiative would:

- o Set a national utility consumption target for 1990; this could be either 50% or 65% of current consumption, depending on how far you want to push this option.

*FRG gets only
9% for oil/900
Georgia 15%
U.S. 33%
(0.1 21%)*

- o Distribute "tickets" for the allowed oil consumption which utilities can trade according to their ability to substitute other fuels;
- o Impose heavy fines for utility oil consumption in excess of "tickets" held by the utility;
- o Provide front-end grants (either \$3.5 billion or \$5 billion depending on the level of reduction) to help utilities finance these new investments. These grants, coupled with the two existing investment tax credits, will provide about 30% of the costs of replacing these oil-fired boilers.

Estimated savings: 750,000 B/D (at a 50% reduction level), 1 MMB/D (at a 65% reduction level).

Budget impacts: \$3.5 billion for the 750,000 B/D level; \$5 billion for 1 MMB/D level. Funds will be available over 10 years.

Cost per barrel saved: \$25 at 750,000 B/D. \$27 at 1 MMB/D.

Discussion

This proposal is designed to overcome utility and public utility commission inertia in moving ahead with capacity expansion to back out imported oil. Utilities have been reluctant to finance capacity additions in excess of actual demand because: utility rates would increase in the short term; oil prices can be passed forward automatically through fuel adjustment clauses; and because of financing problems.

This proposal overcomes these barriers and provides a definite limit on oil consumption through the earlier replacement of existing oil-fired boilers. The transferable "rights" permit the utilities themselves to help determine where to make the capacity replacements. In effect, utilities in areas such as California, where environmental regulations or long coal hauls make replacement capacity costly, would buy tickets from other regions where lower costs would be incurred in switching away from oil. Grants

Less expensive way? Lower grant % and loans vs grants.

and loan guarantees would help make the program more palatable to utilities, public utility commissions and consumers. Utilities could replace oil fired capacity with nuclear, coal, natural gas, or in some cases, possibly solar and conservation. We expect many utilities to choose coal. While utility and public utility commission opposition can be expected, this measure would be applauded by coal producing states. It picks up on a recommendation made by the National Coal Commission. It offers significant opportunities in the near and medium term to increase coal use. Neither the 750 MBD nor 1.0 MMBD oil reduction targets should be particularly difficult to achieve.

B. Synthetic Fuels

For the purposes of this memorandum, synthetic fuels are defined to include: oil shale, coal liquefaction, coal gasification, and ethanol and methanol from biomass. Three levels of synthetic fuels contributions are presented, each of which will draw on some or all of these technologies.

The options for the synthetic contributions are: 500,000 B/D, 1 MMB/D, and 2 MMB/D. These will inevitably be compared with the Moorhead bill which recently passed the House which provided 1.5 MMB/D of synthetics using our definition, and a total of 2 MMB/D including heavy oils. Other organizations and individuals have recommended even higher levels of synthetics by 1990. The National Coal Commission, for example, suggests a 2.3 MMB/D target by 1990. Lloyd Cutler and two coauthors suggested 5 MMB/D by 1990-95.

Syn + heavy = 2 1/2

The Task Force limited the maximum synthetics contributions to 2 MMB/D on the belief that this level represents the upper bound of what can be expected with any certainty from synthetics in the next decade. Many on the Task Force believe that anything over 1 MMB/D is highly optimistic.

The options set out below contain illustrative breakouts of the mix of particular types of synthetics which might be used to reach each target level. If you decide that a Corporation (either inside or outside DOE) should be established to implement the synthetics part of the program, it would be responsible for determining the actual mix.

1. 500,000 bpd Synthetics by 1990

This level of synthetics would entail:

250,000 B/D from oil shale
 170,000 B/D from coal liquefaction
 50,000 B/D from coal gasification
 50,000 B/D from biomass

Budget impacts: \$8 billion.

Approximately 9 non-biomass, and up to 10 biomass facilities would be built.

Discussion

This level of synthetics builds modestly on the initiatives announced in your April 5 speech. For shale, it would rely either on the \$3/barrel tax credit or price or loan guarantee authorities, but not both. For coal liquefaction, it would rely on either federal buys or price guarantees. Loan guarantees would be used for high Btu coal gasification. Biomass -- apart from gasohol -- would also use direct grants and/or loan guarantees. It would require mining of about 50 million additional tons of coal beyond current production (now about 700 million tons). It is a lower level 1990 target than that set in the Moorhead bill as it passed the House (1.5 MMB/D using our synfuels definition, 2MMB/D if heavy oil is included).

This level presents the lowest technical risk since it would permit construction of a limited number of facilities within each category of synthetics, and replication of these facilities would not occur until substantial experience had been gained from operation of this first series of plants. While a corporation could be set up to run a program at this level, a special organization is not absolutely required to meet this target.

Streamlining of the permitting and judicial review processes would help ensure that this goal is met on time, but would not be nearly as important at this level as at the other two discussed below.

2. 1 million Barrels Per Day Synthetics by 1990

This level would involve:

*Why not cleaning
up solid coal?*

250,000 B/D oil shale
550,000 B/D from coal liquefaction
150,000 B/D from coal gasification
50,000 B/D from biomass

Budget impacts: \$27 billion

Approximately 18 non-biomass, and up to 10 biomass plants would be involved.

Discussion

This level of synthetics investment is roughly that implied in the Moorhead bill (1.5 MMB/D excluding heavy oil).* It moves substantially beyond current programs, and would require mining an additional 100-175 million tons of coal above current production. One million B/D synthetics implies significant scale-up of current technologies.

In addition to the financing tools listed for option 1, this level of synthetics would require use of a combination of price guarantees, Federal buys, loan guarantees, and government-owned privately-operated facilities. To achieve this level of synthetics, some streamlining authority would be required to speed up the permitting and judicial review process. Organizationally, some special entity either inside or outside DOE would probably have to be created to assure sufficient private interest and participation to reach the target. Oil shale would be included within the corporation only if the shale developer chose not to use tax credit mechanisms.

3. 2 million Barrels Per Day Synthetics by 1990

This level would require:

400,000 B/D from oil shale
1,300,000 B/D from coal liquefaction
200,000 B/D from coal gasification
100,000 B/D from biomass

Budget impacts: \$63 billion

This option would involve about 30 new non-biomass and up to 20 new biomass facilities.

*Need to set up
advisory committee
similar to Sunday
afternoon group*

*Note, however, that some supporters of the Moorhead bill may view reliance on a heavy crude program of this size (as opposed to true synthetics and non-commercial technologies) as inconsistent with their intent.

Discussion

A 2 MMB/D synthetic program by 1990 would exceed the level of the Moorhead bill by 500,000 B/D. It approaches the maximum technical capacity for synthetics within the next ten years, given possible transportation, resource (particularly water), materials, and other constraints. Many feel it is too high. It would require mining between 250 and 400 million additional tons of coal per year above current production and would involve an even more rapid scale-up of technologies in each of the major synfuels areas than does the 1 MMB/D level.

The financing tools would be the same as those listed in the 1 MMB/D option.

Substantial streamlining of permitting and judicial review requirements would be essential to meet this level of synthetics. Some substantive requirements of existing law would probably have to be waived to reach it. A corporation with a range of financial authorities would be needed, as in option 2, to meet this target.

It is estimated that the per barrel costs of developing synthetics at this level by 1990 would be higher for the last additional 1 MMB/D increment, given the fast pace of development.

but more similar plants may cost less/plant

General discussion of Synthetics

Substantial uncertainty exists concerning the availability of materials, labor and capital for synthetic fuels production. Clearly, to the extent that bottlenecks do develop, this risk increases as the size of the program grows. While work with one model (Bechtel) did not forecast these kinds of constraints (even at the 2 MMB/D level) difficulties may be encountered in actual implementation of either the 1 or the 2 MMB/D which are beyond the sensitivity of that model. Of particular concern are: industrial capacity for heavy castings, forgings, and special products such as thick steel plate; availability of engineering capability for design of shale and liquefaction projects; and construction capacity for large oxygen plants for coal liquefaction. Capital constraints may be felt in the 1-2 MMB/D range, though this is uncertain.

The rapid deployment of a synthetic fuels industry will bring significant environmental impacts, even with strict environmental controls. Some impacts are well known and can be planned for; others are now only partially understood. Expanded coal production for example has problems of land subsidence, acid drainage, and strip-mine reclamation which are recognized. Less well understood are the nature and quantities of pollutants, including potential carcinogens, that may be present in synfuels. Toxic and/or carcinogenic substances may pose risks to both plant workers and consumers if they are present in the final projects, such as gasoline and fuel oil. Shale oil development will produce enormous amounts of waste spent shale, on the order of 250 million tons per year from a 400,000 B/D industry.

*Not much
> oil*

EPA and CEQ point out that the most significant potential long-term risk is posed by accelerated build up of carbon dioxide in the atmosphere. Because of the energy consumed in mining and production, synthetic fuels from coal release 2.3 times as much CO₂ per unit of energy as does the burning of natural gas. If CO₂ has the climate modification impacts that some scientists fear, development of a large synfuels industry considerably increases that risk. This risk is posed not by any of the synfuels options presented in and of themselves, but by the prospect of a much larger program in the future.

The task force paid special attention to reducing possible environmental impacts and attempted to incorporate the cost of significant environmental controls in the overall cost. However, substantial uncertainties remain. Analysis of current environmental laws shows that, with respect to currently regulated pollutants, there should be more than enough sites in this country on which to build the necessary number of synfuels plants. The requirements for water, however, particularly in the arid West, may be critical. Even if sufficient water is available, acquiring the legal rights to use it may be a complex problem and may result in diversion from agricultural purposes to which much of this water is already committed.

Finally, in lightly developed Western areas where much coal and shale is located, the "Boomtown" syndrome -- in which 15,000 to 20,000 new people quickly need housing and services -- may become a problem. Planning and impact assistance, perhaps even beyond the \$150 million per year recommended in your Inland Energy Impact Assistance program, may be needed to ameliorate these effects. This should be reassessed as the program progresses.

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D. Unconventional Oil and Gas

1. Heavy Oils

The U.S. has an estimated reserve of 11 billion barrels of heavy oil, a highly viscous, almost tar-like crude which must be heated to be produced. Much of this reserve is in California. Heavy oils are expensive to produce and refine, though a good product slate can be produced.

This initiative would:

- o immediately decontrol heavy oil; and
- o exempt this production from the windfall profits tax.

Estimated savings by 1990: Decontrol plus windfall tax exemption: 500,000

Budget Impacts: None, since little or no heavy oil would be produced if the windfall profits tax applied, and therefore we would not receive those tax revenues without the exemption.

Cost per barrel: \$28

Discussion

agree | The Moorhead bill, using a Federal buy mechanism, counts on 500,000 bpd of heavy oils to reach its 1990 target of 2 MMB/D. The initiative described here is preferable to price guarantees. Development of heavy oils is basically an extension of new oil development and production technology. The location of reserves is reasonably well-defined. However, the quality of the oil, both in Btu content, and in its high sulfur content, has made investment in heavy oil unattractive. Our estimates of per barrel costs show it to be right at the current world oil price. Subjecting heavy oil to the windfall tax would leave this resource untapped. Exempting it should produce significant import savings.

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While exemption from the windfall profits tax could create a precedent for further exemptions, this case is distinguishable since revenue losses would not be substantial. Treasury strongly opposes the exemption and believes it will encourage other exemptions. OMB, DPS, and DOE disagree on the grounds that little revenue is lost and our original tax proposal was silent on the question of including heavy oil within the tax in the first place.

Some environmental problems are associated with heavy oils, mainly due to emissions from facilities used to generate the heat needed for production. This can be mitigated by an exemption under the Fuel Use Act to permit use of natural gas to fuel the boilers needed to produce heavy oil.

2. Unconventional Gas

There are several potential sources of unconventional natural gas: production from tight sands and Devonian shales, methane gas from coal seams, and geopressurized methane from the pressurized domes in the Gulf of Mexico. Some production from tight sands and deep wells is already occurring. Methane gas has been extracted from coal seams on a very small demonstration basis. Geopressurized methane is known to exist in substantial quantities, though there is currently no production from this source.

An initiative in this area would:

- o Request that FERC deregulate tight sands. Because of definitional problems and time constraints, these were not decontrolled in the Natural Gas Policy Act as other unconventional gas sources were.
- o Commit to seek legislative deregulation if FERC fails to act.
- o Direct DOE to classify gas from tight sands and deep gas as allowable alternative fuels under the coal conversion program. This would allow current oil users to switch to this source and help create a market for this fuel.

What %
is this ?

o Provide a 50¢ mcf tax credit to all new unconventional wells (producing after July 1, 1979), which would phase out at \$26-28 per barrel equivalent of real world oil prices;

750,000

Estimated Savings: 750,000 (with potential for much higher savings -- some estimate up to 2.5 MMB/D) (note: savings assume no geopressurized methane contribution prior to 1990).

1,500,000 ✓
500,000 ✓
1,500,000 ✓
3,500,000

Budget Impacts: Approximately \$1 billion through 1990 (assuming a moderate world oil price trajectory).

Cost per barrel saved: All sources except geopressurized methane: \$20-\$25
Geopressurized methane: unknown

Discussion

The U.S. has potentially enormous unconventional natural gas resources (estimates are as high as 11 trillion barrels). Because natural gas prices have been controlled, little incentive has heretofore existed to exploit these sources. Natural gas has some significant advantages over other fossil fuels in that it is clean-burning, has fewer CO₂ emissions, and it may be lower cost than some of the synthetic alternatives. Tight sands especially hold potential for a lower cost contribution than synthetics. Environmental problems are associated with the drilling and production of some of these gases, particularly geopressurized methane where significant amounts of brine may be produced and other environmental consequences could be substantial. There are also numerous technological risks associated with at least some of the unconventional gas sources.

The deregulation and tax credit approach should provide needed incentives for most gas sources. Treasury opposes use of this (or any other) tax credit on grounds that it is inefficient, it invites tax sheltering, and will distort the competitive relationship with natural gas. DOE, OMB, DPS, EPA, and CEQ believe that these arguments are very much overshadowed by the need to provide a broad-based

market-pull incentive to tap into this potentially very large resource base. More targeted incentives such as a price-guarantee would also have distortions and would not provide as effective an incentive as the tax credit would. A Federal buy or price guarantee approach could also be used. Some additional demonstration wells, particularly for geopressurized methane, will be needed, though the DOE program already provided for fairly high levels of activity in this area. EPA believes that additional resources for technology development and mapping these resources could significantly improve the production potential from unconventional gas by reducing exploration risks. We will work with EPA to better define program needs in this area.

V. DISCUSSION OF OPTIONS AND DECISIONS

Option A - 3 MMB/D Reduction - Modest Synthetics,
Medium Conservation

ADVANTAGES:

$$-\frac{3570}{5} = 714 \frac{0}{10}$$

Would permit 1990 imports to be cut by just over 1/3 at relatively low budget costs and with relatively low levels of technical, environmental and financial risk.

- o Costs per barrel saved are the lowest since conservation and fuel switching costs are generally lower than synthetics costs. If world oil prices do not increase significantly, avoids over-investment in technologies which would not be close to being cost-competitive.
- o Minimizes the institutional issues such as fast-track permitting for projects. Poses fewer conflicts in terms of resource use, e.g., water, land, and materials.
- o Is clearly achievable, probably without fast-track or special organizational arrangements.

DISADVANTAGES:

- o Is clearly not close to the maximum achievable level of import reductions, and provides less protection if oil prices continue to increase (whether steadily or in spurts) over the next ten years. Does not represent a real "call to arms" approach to energy.
- o Falls significantly short of the import reduction/synthetic fuels targets contained in the Moorhead and Jackson bills which have substantial political support in the Congress. It would be characterized as providing little more on the production side than was contained or implied in your April 5 Message.

Option B - 4 MMB/D Reduction -- Stronger Synthetics
Stronger Conservation, Production and Fuel Switching

ADVANTAGES:

- 1090/yr
- o Would cut imports in 1990 in half to a level of 4 - 4.5 MMB/D. This represents a dramatic reversal of current import trends, and it provides a substantial benefit in terms of security, trade and balance of payments if world oil prices increase.
 - o Unlike Option A, is consistent with an import target level of 4 million barrels per day in 1990.
 - o It is a well-balanced program that is both pro-production and pro-conservation. It relies almost equally on conservation and fuel switching, synthetics, and unconventional oil and gas production. Diversifies investments in each of these areas, thereby minimizing risks of failure in any given category.
 - o Minimizes environmental risks while still providing for an active synthetics and coal use program. The natural gas and conservation components of the program provide an environmental cushion which will help in reducing opposition from environmental organizations. The added mass transit investments will be very helpful in this area. The 1 MMB/D synthetics component is strong but achievable. It runs fewer risks of technical, materials, or capital constraints which may increase very substantially as the 2 MMB/D level is approached. If the Corporation finds that an additional 500,000 MMB/D synthetics contribution is achievable it permits you to adopt that at the time the finding is made.
 - o It permits operation of a range of "first generation" plants before committing Federal funds to a substantial number of replicas. This could help keep the overall costs of synthetics down over the longer run, and make them more cost-competitive in the 1990's.

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- o It limits the level of Federal budget risk if synthetics prove less feasible or significantly more costly than now thought. Some believe that the tide will turn against synthetics as more of the financial and environmental risks are received. If this is the case, a synthetics component higher than 1 or 1.5 MMB/D will lack credibility.
- o The 4 MMB/D import reduction target is double the synthetics target set by the Moorhead bill. Although, counting heavy crude, this option falls 500,000 short of the Moorhead bill for synthetics, more than half of total import savings come from production.

DISADVANTAGES:

- I agree with the Congress*
- o On synthetics, it is less ambitious than the Moorhead and Jackson approaches. As such, you are likely to be criticized for not going far enough toward the maximum limit, even with the option of reconsidering an added .5 MMB/D. Fewer coal liquefaction and gasification plants would be built than Moorhead, Wright, Jackson and others would prefer.
 - o It, like Option A and D, runs the risk of a significant congressional battle on utility financing of conservation expenditures, and 1/2 of the conservation savings come from this area. Other measures such as the utility oil backout will also meet substantial opposition.
 - o Curtailment of normal procedural requirements and judicial review will prove contentious in the Congress.
 - o There will be strong, public and environmental opposition both to the production initiatives and to environmental relaxation.

Option C - 4 MMB/D Reduction -- Strongest Synfuels Production Incentives and Fuel Switching

ADVANTAGES:

- o Represents a bold commitment to approach the maximum technically feasible level. In the current pro-synfuels, pro-production climate, it has substantial political appeal and will be seen by proponents of the Moorhead bill as meeting its synfuels goals.

- o By appealing to the clear mood of a majority in Congress and major segments of industry and labor this approach has the best chance of avoiding the congressional haggling which has crippled energy legislation to date, and of enactment roughly as submitted.
- o DOE believes there is a greater chance both of enacting and of successfully implementing the additional synfuels production proposed in Option C than of enacting and implementing the conservation measures which Option B relies on for comparable import reductions.

DISADVANTAGES:

*all Sunday
advisors disagree
with this*

- o The prospects for attaining a 2 MMB/D synfuels component are questionable. As the synthetic fuels debate matures, this may become more publicly apparent than at present.
- o It [^{fails}attempts] to take advantage of the substantial conservation savings which are attainable at relatively low per barrel costs in the residential sector. This is one of the areas which can show near term reductions and help with attainment of 1980-85 import targets. *Wording?*
- o It will increase environmental risks. Water constraints could be serious, and cause greater contention with agricultural and recreational interests. Adverse social impacts in the rural areas of the West will be increased.
- o Will require considerable curtailment of existing legal/regulatory/judicial review requirements. This is likely to prove contentious in the Congress and needed authorities may not be provided.
- o There will be deep-seated and fundamental opposition from environmental, consumer, and some energy commentators. This substantial reliance on synfuels will be criticized by many as a risky gamble and unnecessarily destructive of other values.
- o Increases Federal budget risks, given uncertainties in synfuel costs and world oil prices. May increase the ultimate costs of synfuels in the 1990's due to the strains that reaching 2 MMB/D may place on capital, equipment, labor, etc. Incremental per barrel costs for the last .5 to 1 million barrels are likely to be quite high.

Option D - 5 MMB/D Reduction by 1990ADVANTAGES:

- not true at all*
- o If it could be successfully implemented, it would provide maximum import reduction.
 - o It substantially exceeds any known Congressional proposals in any of the areas that can be used to reduce imports.

DISADVANTAGES:

- o Combines all of the disadvantages of Options B and C, and intensifies some of these impacts.
- o Increases the risks of a credibility gap between what is hoped for and what is achievable under any reasonable discounting for the uncertainties involved in these programs. Given the trade off in credibility, does not greatly enhance the "call to arms" value of a major import reductions program, and may hurt it.
- o It is the most costly to the U.S. Government.

DECISION

_____ Option A - 3 MMB/D Modest Synfuels, Medium Conservation - (not recommended)

_____ Option B - 4 MMB/D Strong Synthetics, Strong Production, Fuel Switching and Conservation (recommended by: OMB, DPS, Kahn and NSC without qualification; CEQ, Interior, EPA recommend but with deletion of authority for corporation to expand beyond 1 MMB/D)

_____ Option C - 4 MMB/D High Synthetics, Strong Production (recommended by DOE. DOE believes Option C is the most likely to be successful through the Congress and implementation. It also believes that to achieve balance, conservation elements should be proposed along the lines suggested in Option B.

*I agree with
This combination
which seems to
approximate option
D.*

_____ Option D - 5 MMB/D High Synthetics, Maximum other (not recommended)

VI. ORGANIZATION

A fundamental issue related to reducing imports is the type of organization and the scope of powers needed to execute a successful synthetic fuels program. Because of extensive government rules that inhibit flexibility, it is unlikely that a traditional Federal agency approach could achieve a 1 or 2 MMB/D target within the desired cost levels and time frames.

The design of a new organization -- corporation or otherwise -- requires a careful balance between the creation on the one hand of a sprawling, powerful institution which is impossible to control and which could create a government monopoly, and on the other hand the creation of an institution of limited power. Most importantly, the new organization must not be given an unlimited life of its own; if the venture fails for any reason, a mechanism should exist to redirect, change or eliminate it.

Three alternative organization designs have been identified:

- Option 1: An Executive Branch corporation with very broad financial and administrative authorities.
- Option 2: An independent government-sponsored enterprise outside the Executive Branch with somewhat fewer financial and administrative authorities.
- Option 3: Similar to Option 2, except that the corporation would have direct ties with the Department of Energy.
- Option 1: Independent Executive Branch Corporation very broad financial and administrative authorities.

The characteristics of the corporation would include:

- o A seven-person Board of Directors with the Chairman appointed by the President to serve a term of 5 years. Three directors would be appointed from outside the government for five-year terms, and the Secretaries

of Defense, Energy and Treasury also would be directors. The compensation of the Chairman and the Board members would be fixed by the President without limitation. Under this option many employees of the corporation would be under Civil Service regulations.

- o A broadly defined synthetic fuels development charter that would include the production of oil from shale, as well as liquids and gas from coal, peat and biomass.
- o A broad range of financing devices, including GOCO, loans, loan guarantees, price guarantees, purchase agreements, participation in joint ventures and equity investments in private firms.
- o Assistance to private concerns for the development of shale oil would be limited to firms for whom the \$3 per barrel tax credit would be insufficient and who chose not to make use of it.
- o Exclusion would be provided from many existing administrative limitations on Federal agencies, such as the Administrative Procedures Act, the Freedom of Information Act, and the Ethics Act.
- o Funding would be provided by \$6 billion in equity and \$40 billion in borrowing and debt guarantee authority which could be outstanding at any one time. The \$6 billion equity would be on-budget; all other funding would be off-budget. (Because of the broad range of financing devices available and the opportunities to turn over debt and equity there arguably would not be an effective limitation on the total funding level or activities over time.)
- o A statutory life of 20 years, unless extended by the President for three additional years.

Option 2: Independent Government-Sponsored Enterprise--
with somewhat fewer financial and administrative
authorities.

This version of the corporation would cover the same range of synfuels production possibilities as Option 1 and would provide all of the financing mechanisms short of those that might allow independent growth beyond current plans and budget authority. This approach however, differs from Option 1 in the following respects:

- o In order to control growth, the range of financing mechanisms available to the corporation would not include participation in joint ventures and equity investments in private firms. Only a limited number of GOCOs would be allowed. Use of the budget authority provided would be on a one-time only basis; no revolution of debt would be permitted. Thus, there would be an effective limit on total spending, unless a further infusion of BA was authorized by Congress and the President.
- o The corporation would have a statutory life of 12 years, sufficient to meet a 1990 goal; at the end of its life, the corporation could be extended or its accumulated liabilities would be automatically assumed by the Treasury.
- o In addition to equity and budget authority similar to the Option 1 corporation, the Option 2 corporation would be given separate loan guarantee authority and also would be authorized to issue up to \$5 billion in low-denomination (up to \$1,000) Energy Bonds so that the public could more directly participate in the synfuels development effort.

good →

Option 3: A Government-Sponsored Enterprise with Direct
Policy and Operational Links to DOE.

This Option is similar to Option 2, but with the following differences:

- o no The corporate structure would consist of the Secretary of Energy as Chairman. The Board would appoint a Chief Executive Officer of the corporation who would be accountable to the Board.

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- o The corporation would receive policy direction from the Secretary of Energy and could tap into DOE personnel for technical and administrative staff.

ANALYSIS

By a wide margin Option 1 would be the most powerful and broad-ranging of the designs. The unlimited budget authority (in practical terms) coupled with a wide range of assistance mechanisms (including equity ventures) would put enormous powers in a corporation independent of the government and off-budget. Its chances of achieving a 1 or 2 MMB/D synthetics goal by 1990, other things being equal, would be very good. Its disadvantages include:

- o The risk that other government incentives such as the oil shale tax credit will be unnecessarily duplicated by additional corporation assistance.
- Serious problem* o The risk that budget costs far in excess of current estimates will be incurred with virtually no way to halt them.
- o The risk that Civil Service coverage will make it difficult for this corporation to hire, promote and fire employees with the necessary flexibility.

Option 2 has the same scope as Option 1, and more targeted and limited financing. This corporation should also be able to achieve a 1 or 2 MMB/D goal by 1990. Being outside the Executive Branch, this corporation would be truly independent, yet its budget authority would have an upper limit and once used would not be restored automatically. Thus, there would be an automatic upper limit on losses in the event of unforeseen technological, environmental or financial problems. The Option 2 corporation's disadvantages include:

- o The inability to assist firms which are also making use of the oil shale tax credit.
- o The risk that much more funding than currently anticipated would be needed to meet the 1990 goal, and that a future President and/or Congress would be reluctant to provide it.

The only major difference between Options 2 and 3 is that Option 3 provides closer policy ties with the Department of Energy through having the Secretary of Energy as Chairman of the Board. The major disadvantage is that the Corporation will be less independent from Congressional pressures that can be exerted on the Secretary of Energy.

DECISION

- o Option 1 (recommended by Treasury, NSC) _____
- o Option 2 (recommended by OMB, DPS, CEQ,
EPA, Interior, Kahn) *= Energy Bonds* ✓ _____ **J**
- o Option 3 (recommended by DOE) _____

FOREIGN ACTIVITIES

You also need to consider whether the corporation should be precluded from participating in ventures outside the United States. (Both Options 1 and 2 below would allow the corporation to participate in any otherwise qualified domestic U.S. venture, regardless of financial participation by foreign interests.)

Option 1

The corporation should not be precluded from operating outside the United States, unless the Congress insists that this be done. Otherwise, if queried by the Congress, we should reply that in order to assure that the Corporation's activity will be largely focused on exploiting resources within the United States, Presidential approval of any venture outside the United States or of foreign participation in any venture in the United States would be required.

- o We should not deprive ourselves of the opportunity to tap foreign financial resources to exploit physical resources outside the United States, e.g., Canada or Venezuela, as recommended to you by Arthur Burns.
- o The real objective of this exercise is to reduce oil imports from OPEC and to help the entire industrialized and developing world develop alternative energy sources. This requires worldwide activity, not merely U.S. ventures.
- o The Tokyo Summit Declaration envisages the possibility of financial participation in projects which are international in scope; the corporation is one appropriate means to implement that commitment for the United States. Legislation which precluded the corporation from performing this function would strike our Summit partners inconsistent with the Summit agreement.

Option 2

The corporation should be precluded by law from participating in ventures outside the United States. (The corporation could participate in U.S. domestic ventures with foreign entities.)

o The goal of the corporation is to develop a domestic capacity for synfuels production in connection with our import reduction effort, not to develop or demonstrate on a domestic or international basis alternative energy technologies.

We should develop these options

o Many other mechanisms are or can be made available to meet the Tokyo commitment, and those ought to be used. We can reassure our Summit partners in advance of any announcement on this point; after all, the Tokyo agreement on technology development was a U.S. initiative.

o Giving the corporation the authority to invest windfall profits tax receipts abroad will make it more difficult to persuade the Congress to enact either the tax or the corporation.

o This corporation, whether located inside or outside the Executive Branch, will be independent of the President, who has the Constitutional responsibility to conduct Foreign Affairs.

DECISION

- o Option 1 (recommended by NSC, DOE, and State) _____
- o Option 2 (recommended by OMB, DPS and Kahn) _____ ✓ J

VII. PERMITTING AND JUDICIAL REVIEW: THE "FAST-TRACK" ISSUE

This section addresses the principal issues involved in expediting the regulatory and permitting procedures that apply to any major new energy project. You should consider these issues in conjunction with your decision on synfuels program size, because the current processes for expediting decisions on these facilities probably are not adequate to handle an ambitious 1990 synfuels production target.

The five options regarding permitting and judicial review range from generally maintaining the status quo to providing an Energy Mobilization Board (EMB) with override authority while precluding judicial review with respect to most Federal, State and local determinations on critical energy facilities. As with the imports reduction options themselves, these options represent discreet points on a continuous spectrum; any number of other options could be formulated using different combinations of these measures.

Option 1: Use Existing Mechanisms

Your Administration has taken a number of actions within the last year to facilitate the permitting and construction of critical energy facilities. These include:

- o By Executive Order in April 1979, a Critical Energy Facility Program was established under the direction of OMB.
- o CEQ has issued regulations (effective July 30) reforming the administration of the National Environmental Policy Act. These regulations create a coordinated environmental impact statement process with, among other things, time limits and the use of joint Federal and State hearings and impact statements.
- o By Executive Order, the Energy Coordinating Committee was established.

- o EPA has taken significant steps to consolidate all Federal environmental permit actions and procedures under four separate statutes, and several interagency agreements to facilitate permitting have been signed.

Option 1 would rely on existing authorities and the setting of publicly available target dates. Increased emphasis would be given to the efforts listed above. The following additional actions would be taken:

- o Standardize permit issuance procedures for all critical energy facilities.
- o Assign a lead agency for each project to negotiate target dates for completion of all Federal permits, publish target dates in the draft EIS, and to establish procedures for coordinating Federal and State EIS preparation and other decision schedules.

Under this option, there would be no change in judicial review procedures.

PRO:

- 1) No need for legislation, and no start-up delays from passage of new legislation.
- 2) Need for more drastic steps, particularly at the Federal level, has not been conclusively established. The OMB review of coal-fired power plant permitting by Federal agencies has not yet revealed any significant delays.

CON:

- 1) Does not allow, in all likelihood, the success of an accelerated synfuels development program.
- 2) Does not address the widespread perception that drastic remedies are needed.

Option 2: Expedited Permit Reviews and Expedited Judicial Review

We have done nearly everything we can under existing authorities to reduce needless delay in the permitting of

Critical

critical energy facilities, but we probably need to make changes in existing law to accelerate their development. Under this option, which would require new statutory authority, the Federal approval process for critical energy facilities would be modified by increasing the authority of the Executive Branch -- through a new "Energy Mobilization Board" (EMB) -- to take several accelerating actions.

This option is the closest to the Dingell, Udall and Jackson legislation pending in Congress.

The new legislation would:

- o Create the EMB in the Office of the President with three members whose nominations would be confirmed by the Senate.
- o Authorize the EMB to designate certain non-nuclear energy facilities as "critical" and to establish binding decision schedules for Federal agency action (which could in cases of "exceptional national need" be shorter than existing time limits, but not less than 1 year).
- o In order to increase the likelihood that States would comply with the accelerated decision schedule, provide fiscal incentives to States to help them complete their permitting process not later than the Federal schedule.

Except where there is a Constitutional issue, prohibit judicial review of EMB decision to designate a "critical energy facility" and provide a 60-day statute of limitations for bringing cases challenging an agency decision on the permit application itself.

- o Consolidate judicial review of all Federal permitting decisions in the Court of Appeals for the Circuit in which the project is located, and require that Court to expedite its review and decision.

PRO:

- 1) Addresses perception of need for change and is most similar to pending legislation in Congress.

Needs Presidential involvement (as with ITC, CAB, etc)

?

need ?

- 2) By leaving in place substantive requirements such as "best available technology" requirement and emissions limitations, could add to costs of synfuels plants -- but should not actually prevent their location and construction.

CON:

I agree

- 1) Fiscal incentives for state and local cooperation may not be effective and should not be necessary.
- 2) By leaving in place substantive requirements such as Clean Air Act, "best available technology" requirement, emissions limitations, and substantive state and local requirements could add to costs of synfuels plants -- but should not actually prevent their location and construction.

Option 3: Increased EMB Authority over certain Federal, State, and local decisions and more circumscribed judicial review

In addition to the steps taken under Option 2, this Option would seek additional statutory authority for the EMB to:

- ok* o Make decision schedules for (but not preempt) state and local as well as Federal agencies mandatory.
- ok* o Allow the EMB to make permit decisions when a Federal agency failed to act in accordance with the established schedule (EMB would apply Federal law) and when a state or local agency failed to act (EMB would apply state or local law).
- ok* o Provide the EMB with the authority to waive procedural (only) requirements of Federal, State or local laws governing a critical energy facility (CEF) and to hold a CEF harmless from changes in substantive or procedural requirements after commencement of construction (on a plant-by-plant, requirement-by-requirement basis).

but only with President's concurrence

ok if President
 concurred (22?) o / no
 Judicial review of EMB waivers, in the absence of a Constitutional issue, would be prohibited.

PRO:

- 1) The pace of state and local action often can be the critical factor in determining whether a CEF is delayed. This Option provides additional leverage without wholesale abandonment of environmental or other principles.
- 2) To the extent regulatory uncertainty is a factor in slowing down or discouraging participation in synfuels development, the hold harmless ("grandfathering") authority will improve the prospects for the program's success.
- 3) Other arguments in favor of Option 2.

CON:

- 1) Will be strongly opposed by environmental and other private organizations, and goes well beyond the Udall, Dingells, Jackson bills.
- 2) "Buck-passing" by regulatory agencies to EMB may be encouraged.
- 3) Extensive limitations on judicial review impact on important part of government process, and that safety valve should not be tinkered with lightly.
- 4) "Grandfathering" may result in vital new public health regulations not applying to major energy facilities.

Option 4: Increased EMB Authority

In addition to the steps taken under Option 3, this Option would seek additional statutory authority to:

- o Provide the EMB with authority to waive substantive as well as procedural requirements of Federal laws governing a critical energy facility, subject to disapproval by a Joint Resolution of Congress within a time certain.

- o All judicial challenges would be consolidated and expedited in the Temporary Emergency Court of Appeals (TECA).

PRO:

- 1) Additional authority to waive substantive Federal requirements would provide additional leverage.
- 2) Consolidation of all judicial review in TECA would make expedited handling of cases more likely in fact.
- 3) Other arguments in favor of Option 3.

CON:

- 1) Additional resources and expertise would have to be provided to the President or the EMB to handle complicated waiver decisions on complicated facilities.
- 2) Potential abuse through wholesale waiver of substantive statutory requirements by future administrations less sensitive to legitimate environmental concerns.
- 3) Other arguments against Option 3.

Option 5: Future Preemption of State/Local Authorities

Waiver authority over procedural and substantive Federal requirements would not necessarily assure the attainment of energy production goals, because of potential delay over substantive impasses at State and local levels. For example, issues related to water rights in Western states would still be resolved by State authorities.

This Option, therefore, would apply all of the provisions of Option 4, including the EMB waiver authority for substantive requirements, to state and local government actions.

In addition, no action or decision involving a critical energy facility could be preliminarily enjoined by the Court of Appeals except at the request of a Federal agency.

PRO:

- 1) Provides the most absolute assurance that critical energy projects could move ahead without delay.
- 2) Other arguments in favor of Option 4.

CON:

- 1) Opposition from States, local governments and environmental groups could be overwhelming.
- 2) Other arguments against Option 4.

DECISION

- o Option 1 (no recommendation) _____
- o Option 2 (recommended by Justice, DEQ Interior, EPA) _____
- o Option 3 (recommended by OMB, DPS, NSC, * Kahn) _____ ✓ ▽
- o Option 4 (recommended by Treasury, DOE) _____
- o Option 5 (no recommendation) _____

** See notes p 40, 41*

VIII. Quotas backstop import targets.

The issue was raised at Camp David whether some formal mechanism should be established for ensuring import reductions. This section of the memorandum addresses your authority to set an import quota and recommends that you state your intent to do so for 1979 and 1980.

Authority

Section 232(b) of the Trade Expansion Act provides you with a range of authorities to act to limit or otherwise deal with imports which threaten national security. Upon a finding by the Secretary of the Treasury that import levels constitute a threat to the national security, you may set import quotas (or fees) under 232(b). Secretary Blumenthal has made these findings as recently as March 14, and you are free to set a quota now without any further procedural requirements.

This is the most direct authority available to you. We have not had time to research whether other options are available under other laws.

Implementation of a quota system raises a series of issues which we have not been able to address in the short time since this suggestion was first raised. While we foresee no difficulties in meeting an 8.5 MMB/D quota in 1979 and 1980, the questions about what mechanism we would use to enforce it will undoubtedly be raised. An auction system which sells "tickets" or rights to import is one possibility; use of our gasoline and other product allocation authority is another. Both, however, present some difficulties in implementation.

Options

1. You could act now to set a quota for 1979 and 1980 at a level of 8.5 MMB/D, and announce your intent to use this mechanism on a year by year basis to ensure that import targets are not exceeded. You would not, however, set quotas for any of the years beyond 1980.

2. You could set targets now for each year between now and 1990.

Discussion

Neither CEA nor DOE foresee any difficulties in meeting an import quota of 8.5 MMB/D this year or next, even under optimistic economic growth forecasts. There is substantially more uncertainty, however, in the post-1980 period, particularly in 1982-84 about what levels could be met. At this time, we do not recommend that you go beyond Option 1 in specifying the actual quota levels, though we see no problems with announcing a general policy of setting yearly import quotas to backstop our targets.

Secretary Blumenthal and Henry Owen strongly believe that announcing a 1979 and 1980 quota now would have significant beneficial impacts on the dollar. The State Department feels that this action would be welcomed both by our OECD allies and by some of the OPEC nations, if it were properly explained. DOE, DPS, and OMB believe that it would help underscore the public's perception of the seriousness of your overall energy efforts here at home, and would be well received by the Congress (though this latter point needs further checking).

To deal with the implementation question, you could ask DOE and Treasury to report back to you within 30 days on mechanisms for enforcement of the quota.

Decision

✓ _____ Announce 1979 and 1980 quota levels of 8.5 MMB/D, state a policy of using this mechanism to assure that we meet future targets, and direct DOE and Treasury to develop implementation mechanisms. (Recommended by: DPS, NSC, Treasury, State, and OMB) ✓

_____ Announce year by year quotas beyond 1980. (Not recommended by any agency)

_____ Defer decision.

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CEO MEMO

EXECUTIVE OFFICE OF THE PRESIDENT
COUNCIL ON ENVIRONMENTAL QUALITY
722 JACKSON PLACE, N. W.
WASHINGTON, D. C. 20006

11 July 1979

MEMORANDUM FOR THE PRESIDENT

FROM: GUS SPETH, ACTING CHAIRMAN



SUBJECT: OIL IMPORT REDUCTION DECISION

One of your most important decisions is what changes you make in the environmental permitting process to accelerate decision making. There is a clear and exceedingly important distinction between Options 2 and 3 in the decision memorandum.

Option 2 makes basic procedural and management changes which will accelerate environmental permitting without waiving basic environmental protection standards. Option 2 is most consistent with the Udall, Dingell and Jackson "fast track" bills. Option 2 adopts the approach of wringing the delay out of the review process, and I strongly support it.

Option 3, on the other hand, provides for waivers of certain federal environmental protections, including the National Environmental Policy Act and also public hearing requirements. It also prohibits judicial scrutiny of these waiver decisions, thus eliminating the traditional check on abuse of agency discretion. These fundamental changes in the existing environmental protection scheme, which you have strongly supported, are unnecessary to get the job done and would raise serious political issues with your environmental constituency.

Several Administration studies have demonstrated that environmental permitting requirements are not a major cause of delay and are not on the critical path. The principal delaying factors for major energy facilities are equipment availability, materials shortages, labor disputes and fiscal matters.



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

July 11, 1979

J called Jim
J

MEMORANDUM FOR THE PRESIDENT

FROM: Jim McIntyre *J*
SUBJECT: Trade Reorganization: Import Relief

You have expressed concern about one aspect of our trade reorganization proposal: whether import relief functions, if placed in the Commerce Department, would be subject to a protectionist bias.

I doubt that antidumping and countervailing duty cases would be subjected to a strong protectionist bias in Commerce for three reasons. First and foremost, the new antidumping and countervailing procedures contained in the MTN bill greatly reduce the amount of discretion available in the decisions. Thus, even if there is a protectionist bias in Commerce, the law should largely insulate these procedures from it. Second, in those areas where there is policy discretion, our proposal to expand the Trade Policy Committee's oversight of such matters would further assure evenhanded treatment. Finally, we envision placing import relief in an international trade unit reporting to an Under Secretary for Trade and insulating the import relief functions from Commerce's business advocacy activities.

In addition, we are not convinced that Commerce has such a bias today. As Secretary Kreps has pointed out in her June 21 memo to you, a review of 28 import relief cases shows that Commerce and STR cast identical votes on 24, and that on the remaining four, STR voted to deny relief in two (non-rubber footwear and bicycle tires) and Commerce voted to deny relief in the other two (unwrought copper and high carbon ferrochromium).

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Further, Commerce voted to deny import relief in 18 of the 28 cases. This behavior is not surprising, given the diversity of business views regarding free trade. While many protectionist elements of business look to Commerce as a protector, free trade elements such as exporters and retailers also are important constituents of the Department and many of them favor this move.

The alternative to placing import relief decisionmaking in Commerce is to move it to STR as Bob Strauss suggests. This would remove any appearance of protectionist bias, be popular on the Hill, but increase the EOP size by at least 85 people and be opposed by organized labor.

MEMORANDUM

THE WHITE HOUSE

WASHINGTON

July 11, 1979

INFORMATION

MEMORANDUM FOR: THE PRESIDENT
FROM: HENRY OWEN *HO*
SUBJECT: Trade Reorganization

The risk that transferring the countervailing duty and anti-dumping functions to Commerce will produce a shift toward protectionism can be reduced by taking two actions:

1 - stipulating, as the McIntyre-Strauss proposal provides, that the Trade Policy Committee will "coordinate" Commerce's administration of import relief measures, to the extent legally appropriate;

2 - subsequently directing the chairman of the Trade Policy Committee to review each Commerce decision on countervailing duty and anti-dumping cases in the Committee -- not in order to over-ride Commerce's decisions, which would subvert the law's intent, but to bring to your attention the trade policy implications of significant decisions and to recommend legislative action if necessary to reduce rigidities in the new law governing these import relief measures.

John Moore continues to support the Treasury-State option. He favors giving STR an expanded export promotion mission by having it operate 12 or 13 small regional trade centers abroad, in close conjunction with Eximbank. He would use private sector people (e.g., retired CEO's) and the best of State's commercial attaches to staff these offices.

He continues to feel that Commerce should not be given an expanded trade role. He feels the Department is too industry related and service oriented and he questions its competence. If import relief functions are placed in Commerce, he would reduce the possibility of protectionist bias by separating import relief adjudication from investigation and prosecution. The latter he would give to Commerce, the former to either Treasury or STR.

He recognizes that giving STR import relief adjudication and expanding its export promotion mission would increase the EOP staff but he feels this political cost is outweighed by the political benefit gained in the international business sector.



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

MAY 10 1979

*Susan
hold
J*

MEMORANDUM FOR THE PRESIDENT

FROM: Jim McIntyre *Jim*

SUBJECT: Summary of Memorandum on Reorganizing the Trade Functions of the Government

This paper is a summary of a longer memorandum (attached) seeking your guidance on trade reorganization. The memo, which has been circulated several times to the agencies, discusses export promotion, import relief, trade policy direction, and trade negotiation, offering various options with respect to each.

Bob Strauss would like you to defer a decision on trade reorganization at least until after the House-Senate conference on MTN May 22-23. He feels that a decision on a trade department -- which is likely to fall short of the Roth-Ribicoff bill -- will anger these key Senators at the time we are asking them to support us in fighting off protectionist pressure on specific aspects of the MTN legislation from House Ways and Means. Such a decision, he thinks, may also turn the MTN conference into a debate on the specifics of trade reorganization -- which may harm MTN on the floor. <

Bob therefore recommends that you defer any decision on trade reorganization for the time being and that he use this hiatus to persuade Ribicoff, Roth and the Senate Finance Committee to accept a flexible commitment on trade reorganization that does not commit us to any specifics about a trade department.

There are several flaws in this approach:

- ° You and I have promised Ribicoff an Administration position on trade reorganization by the beginning of May.

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- ° Ribicoff may not react negatively to your trade decision, unless you reject the trade department altogether. He expects that the trade reorganization initiative will be by legislation with ample opportunity for him to amend.
- ° Ribicoff is unlikely to back off his announced intention to seek an Administration commitment to at least some of the specifics of a trade department in the MTN legislation. The Senate Finance Committee voted this week to ask the Administration to commit in the MTN legislation to all of the specifics of Roth-Ribicoff. In hearings and a conversation with Harrison Wellford on Tuesday, and at his retirement press conference on Thursday, he reiterated his firm intention to create a trade department, to get a commitment for it with MTN, and to hold hearings on it this summer while MTN is pending. Consequently, before we can negotiate MTN language on trade reorganization, we must have your guidance on the specifics.

Therefore, OMB recommends that you make tentative decisions but not circulate the decision memo, and that you convey your views to Strauss and me only. We would then meet with Ribicoff to discuss the timing of MTN and trade reorganization, and our staffs would meet with Ribicoff's staff to negotiate language for the MTN legislation that keeps your and his options open in areas where your reorganization concept differs from the Roth-Ribicoff bill.

Decision:

_____ Decide now, announce now:

_____ Make tentative decisions now as guidance for negotiations with the Congress (supported by OMB). DPS & CL

_____ No decision now, other than a general promise to the Congress to supply within 60 days after MTN legislation is enacted a proposal to strengthen trade organization (supported by Strauss, Owen/NSC).

Although there is contention about individual transfers, there is a general consensus among your advisors and the affected agencies that:

- (1) there should not be an additional Cabinet department for trade;
- (2) STR should remain in the Executive Office, at least to coordinate policy;

- (3) nonagricultural export promotion functions, including the Export-Import Bank (Eximbank), should be strengthened and moved to Commerce;
- (4) post-MTN monitoring and implementation functions should be placed in Commerce;
- (5) the mandate of the Trade Policy Committee should be expanded; and
- (6) trade negotiation responsibilities should remain with STR.

Exceptions to this general consensus are noted in the individual decision boxes that follow:

Introduction

Major U.S. trade functions are located in a number of agencies. The Special Trade Representative (STR) has a lead role in the trade agreements program, but many issues are handled elsewhere, and in most instances trade is not the principal concern of any agency where trade functions are located. Our recent trade difficulties and -- currently -- the submission of the multilateral trade negotiations (MTN) package to the Congress have heightened public interest in trade and brought demands for changes in our trade organization.

Although the U.S. is the only major industrial nation without a Cabinet-level trade department, organization is not the primary cause of our trade problems. Rather, such competitive disadvantages as higher-cost labor, inefficient facilities, changing market demands, and legal and policy disincentives (e.g., antitrust, minimum wage, tax incentives, concerns for human rights, the environment, and national security) render U.S. industry often unable to meet foreign competition. Further, some critics of current trade organization seek to move functions in the hope that the new setting will either afford trade a higher priority or give the critics' concerns a more sympathetic hearing. For example, those who believe that Treasury is dominated by "free-traders" and therefore does not enforce the import relief laws aggressively would like to move those functions to Commerce or a new trade department. On the other hand, reorganization may ameliorate some of the problems and, given the MTN agreement, it is important now to signal the government's commitment to tough enforcement of the codes.

Political Assessment

In general, business would like to see trade concerns represented more aggressively in the Executive Branch. The National Association of Manufacturers strongly supports the Roth-Ribicoff proposal, the Chamber of Commerce favors building on Commerce, and the Business Round Table takes no position. The AFL-CIO takes no formal position now, though they are concerned about anything too ambitious either in terms of building on Commerce or creating a new department; they do, however, have complaints about the performance of State, Treasury and Eximbank.

As you know, there is significant support for trade reorganization in the Senate. In the House there is little active support to date for any significant reorganization of trade functions. Those supporting structural change prefer creation of a new department and most do not seem especially fond of building on Commerce as a second choice.

I. Export Promotion

Strengthening our export promotion programs is a substantively logical and perhaps politically imperative step. MTN provides an attractive opportunity for change.

Export-Import Bank

The principal trade financing agency is the Export-Import Bank (Eximbank). Although generally credited with doing a good job, Eximbank has been criticized for supporting trade promotion where there is little foreign competition and where other commercial financing is readily available. Eximbank now has a full-time, Presidentially appointed board. In addition, it receives policy advice from a National Advisory Council (NAC) composed of Treasury, Commerce, State and the Federal Reserve Board. Two options (other than the status quo) are presented with regard to Eximbank:

1. Place Eximbank in Commerce, subject to the direction and control of the Secretary but still managed by the Board. The Secretary of Commerce would replace the Eximbank President as Chair of the Board (though the President would continue as chief executive officer). This is similar to the Commodity Credit Corporation's arrangement in the Department of Agriculture. This change would increase consistency between Eximbank activities and our overall trade policy and would signal a strong commitment to export development. On the other hand, it would diminish the advantages of having an "anonymous buffer" provided by an independent bank and could imperil the objectivity of Eximbank's credit decisions should promotional considerations become paramount.
2. The Secretary of Commerce would chair the Eximbank Board, but the agency would not be moved into Commerce or placed under the direction and control of the Secretary. This would increase Executive Branch policy guidance without moving Eximbank but could compromise slightly the decisionmaking independence of the Board.

Decision:

Option 1. Move Eximbank to Commerce

(Supported by CEA, DPS, OMB, Pettigrew, Commerce, Labor, Treasury)
Watson & CL

Option 2. Appoint the Secretary of Commerce Board Chair of an independent Eximbank

(Supported by State; acceptable to Eximbank)

Option 3. No change in status or Board composition; create an interagency advisory group headed by Commerce

(Supported by Eximbank; Owen/NSC support this option provided Commerce chairs the NAC)

State's Commercial Officers

The performance of the Commercial Officers is criticized because this function is subordinated to economic reporting in State and attracts less capable Foreign Service Officers. Further, critics argue that the skills, training and career aspirations of diplomats are inconsistent with the job requirements for Commercial Officers. Those who believe that this function should remain in State contend that economic reporting and commercial activities are handled jointly in our embassies and should not be separated. Two options are presented:

Option 1. Move the Commercial Officers to Commerce. This move would put both domestic and overseas export promotion staffs under one agency that emphasizes expanding U.S. exports. Further, it would attract people interested in representation, rather than career diplomats, and would be appreciated in Congress (it is proposed in both the Byrd and Roth-Ribicoff bills). Those opposing this move contend that it would result in wasteful duplication of effort and unnecessarily increase staff requirements. And the move would require a complicated personnel change that would take some time to effect.

Option 2. Improve the performance of the Commercial Officers, but retain them in State. Commerce and State would conduct a number of planning, program and review functions jointly, and Commerce would have a formal, equal role in selection, training, and personnel management of Commercial Officers. This would avoid the disruption of moving personnel or positions from State. On the other hand, it is similar to previous unsuccessful agreements to improve State's commercial performance, would still leave State with primary control over the officers, and would not satisfy those on the Hill and elsewhere who want to see commercial representation in a trade-oriented agency.

Decision:Option 1. Move the Commercial Officers from State to Commerce.

_____ (Supported by CEA, DPS, Pettigrew; OMB supports on condition that only enough officers to handle our major trading partners are transferred; acceptable to Commerce) & CL

Option 2. Retain the Officers in State, but strengthen Commerce's role in managing them.

_____ (Supported by Owen/NSC, State, Treasury; acceptable to Commerce) Watson

Post-MTN Monitoring and Implementation

The consensus is that all MTN monitoring and implementation responsibilities be located in Commerce. This would assure consistent monitoring by an agency for which trade is a primary concern and that has an adequate supporting staff.

Decision:

_____ Yes (supported by OMB, Owen/NSC, Pettigrew, Commerce, State, Treasury) Watson

_____ No (supported by DPS, Agriculture and Labor, who favor maintaining post-MTN monitoring and implementation in the agencies with individual expertise) & CL

II. Import Relief

Import relief functions are directed by several agencies. The Trade Policy Committee and other interagency bodies with varying membership supervise some of these functions, while others are subject to little, if any, interagency coordination. Critics complain that this dispersion of responsibilities greatly complicates and retards efforts to obtain import relief. Further, export functions are in large measure separated from import functions, even though dealings with other nations frequently encompass both import and export matters.

Antidumping and Countervailing Duty (CVD) Cases

The most criticized import administration activity is antidumping and countervailing duty (CVD) cases in which foreign producers are accused of receiving subsidies or selling at less than fair market value. The new

CVD and antidumping codes resulting from the MTN will require administrative changes, and congressional satisfaction with the Administration's plans to enforce these codes will be a critical element in securing MTN passage. We offer two options:

- Option 1. Retain in Treasury, but subject the activities to interagency coordination and increase resources. This would give other agencies a chance to comment, keep the function near Customs, draw on Treasury's expertise, not run the risk of increased protectionism, and be less disruptive than a transfer. But, it is unlikely to satisfy private sector and congressional critics of Treasury.
- Option 2. Transfer these functions to Commerce, which would increase the likelihood of faster, more vigorous enforcement, help satisfy congressional pressure, and locate import and export controls in the same place. Conversely, a transfer would separate the functions from Customs, which is best placed to secure the necessary information and which collects the duties assessed; also, many critics of Treasury disagree not with its administration, but with its reputation for non-protectionist policies.

Decision:

- Option 1. Retain in Treasury, but provide for interagency consultation and increase resources.

(Supported by CEA, DPS, OMB, Owen/NSC, Agriculture, State, Treasury) & CI

- Option 2. Transfer the CVD and antidumping functions to Commerce (with interagency consultation).

(Supported by Pettigrew, Commerce) Watson

Unfair import practice cases (International Trade Commission)

Section 337 of the 1930 Tariff Act authorizes the ITC to apply sanctions for unfair import practices. ITC recently has expanded its activities and has been entering into some agreements that are inconsistent with U.S. trade policy or duplicative of other enforcement functions, but that the Administration can review only after they are concluded. Senator Long's interest in the ITC focuses on functions other than this one, and the Roth-Ribicoff bill proposes to move it to a new trade department. Transferring this authority to Commerce would bring it under Executive Branch control and would be an appropriate part of a consolidation of trade functions, but it would abolish a healthy multiplicity of relief measures and might run into some opposition in Congress and the private sector.

Decision:Transfer ITC's Section 337 authority to Commerce.

_____ Yes (supported by Owen/NSC, Pettigrew, Commerce) Watson

_____ No (supported by CEA, DPS, OMB, Agriculture, State, Treasury) & CL

Import-related operational functions of STR

STR has a number of import relief functions. They are not central to STR's mission and are principally staffed by Commerce and State. The memo offers the option of transferring these functions to Commerce on the grounds that they are line functions inappropriate for the Executive Office. Some argue that their presence in STR might harm its reputation for objectivity, though this has not been a problem in the past. Others contend that many import relief cases concern agricultural products and therefore should not be handled in Commerce.

Decision:Transfer STR's import-related operational functions to Commerce.

_____ Yes (supported by OMB, Pettigrew, Commerce) Watson

_____ No (supported by CEA, DPS, Owen/NSC, Agriculture, Labor, State, Treasury) & CL

III. Trade Policy Direction

Much, but not all, trade policy is coordinated through the Trade Policy Committee (TPC) and two committees functioning beneath it. While policy coordination has worked well on the whole, some complain that important trade policy issues are not addressed through the TPC mechanism. The memo suggests bringing three additional functions within the purview of the TPC:

1. Currently there is no interagency coordination of countervailing and antidumping duty functions. Because the execution of functions is in some measure adjudicatory, the case-by-case fact-finding and adjudication would remain in either Treasury or Commerce. TPC review would center about coordination with other trade matters and timing of decisions.

Decision:Include under TPC.

_____ Yes (supported by CEA, DPS, OMB, Owen/NSC, Pettigrew, Agriculture, Commerce, Labor, Treasury) Watson & CL

_____ No

2. Negotiation of commodity agreements is handled by State and subject to an interagency mechanism different from the TPC. Adding them to the TPC's jurisdiction would increase the consistency of overall trade policy and would assure that all affected interests would have a voice in decisions; on the other hand, it might complicate commodity issues that have implications beyond trade (e.g., North-South dialogue).

Decision:

Include under TPC

- _____ Yes (supported by CEA, OMB, Owen/NSC, Pettigrew, Agriculture, Commerce, Labor) Watson
- _____ No (supported by DPS, State, Treasury) & CL

3. Energy trade issues are now resolved by Energy and are the subject of some complaints of lack of coordination. These are included in the Byrd bill for consolidation into a trade department, though it can be argued that the special nature of energy issues calls for only special DOE expertise.

Decision:

Include under TPC

- _____ Yes (supported by OMB, Pettigrew, Agriculture, Commerce, Labor, Treasury) Watson
- _____ No (supported by CEA, DPS, Owen/NSC, Energy, State) & CL

NOTE: Labor strongly recommends that full representation be assured on other interagency trade policy committees including East-West trade, international investment, Eximbank's National Advisory Council, and other interagency trade policies not now coordinated by STR. Owen/NSC would include coordination of trade adjustment assistance and all import relief.

IV. Trade Negotiation

Trade negotiation lead responsibilities are now divided among STR, State, and Treasury, which may make it more difficult to achieve consistency in our trade relations with other governments, to exploit leverage among different negotiations with the same country, and to avoid having other countries play U.S. agencies against one another. Two options are presented:

- Option 1. Maintaining the status quo, with STR continuing its existing negotiating and coordinating roles, on the theory that the system is working adequately now. This would leave existing a system that requires extensive coordination and might not take full advantage of potential leverage available when there is unified responsibility for all negotiations with a given foreign country.
- Option 2. Consolidating all trade-related negotiations in Commerce, which would ensure one U.S. voice in trade negotiations and maximize leveraging potential, but would separate some trade negotiations from non-trade negotiation linkages and would not obviate the need for an Executive Office coordinator. Removing STR's negotiating responsibilities could be viewed as "gutting" STR and would be unacceptable to those who favor a strong STR.

Decision:

- Option 1. Continue STR's existing negotiation and coordinating roles.

_____ (Supported by CEA, DPS, OMB, Owen/NSC, Agriculture, State, Treasury) Watson & CL

- Option 2. Consolidate trade-related negotiations in Commerce.

_____ (Supported by Pettigrew, Commerce)

THE SPECIAL REPRESENTATIVE FOR
TRADE NEGOTIATIONS
WASHINGTON

May 11, 1979

MEMORANDUM

TO : The President
FROM : Robert S. Strauss 
SUBJECT: Trade Reorganization

The last word I had with Abe Ribicoff was that he was very unimpressed with what he understood the Administration would probably present in the way of reorganizing the trade area of the U.S. Government. He also felt that most of the rest of the Senate Finance Committee and Government Operations Committee would be even less sympathetic than he would be to the range of proposals that he felt were live Administration options based, I guess, on his conversations with Jim McIntyre.

In my judgment, an Administration proposal that would be likely to emerge based on the draft OMB memorandum that I have seen would be likely to be rejected by the Congress. In my judgment, it would also create interagency and private sector jealousies and disputes.

At this stage, I believe that Ribicoff would accept a reasonably flexible outline of the type of proposal the Administration will submit, as long as there is language in the MTN legislation calling for a formal proposal to be submitted within 60 days of passage of the MTN bill. While I do not know whether we will be able to improve on the reorganization proposal in the interim, if we follow this procedural proposal we will at least be in a position to postpone some of the negative aspects of what is likely to be an acrimonious debate until after the MTN legislation is out of the way.

This may be a selfish attitude on my part--in fact it probably is a selfish attitude on my part--but I think this is a reasonably objective assessment and does present a fair picture. I believe that we can get by without a new department if we handle it correctly. I seriously doubt that we can get by without a new department if we present a proposal that falls far short of Hill expectations.

Now that it has been announced that I am leaving STR, there are some additional points that I would like to make on the substance of trade reorganization. I have held long conversations with a number of people, and particularly with my Deputy, Alan Wolff, who probably knows the trade area in the government as well as anyone, as he was the chief draftsman of the 1974 Trade Act under which we operate.

The reason that Wilbur Mills prevailed upon Jack Kennedy to establish the position of Special Trade Representative in 1962, was that there was a distrust of the State Department and a suspicion that foreign policy concerns might dominate the conduct of U.S. trade policy. It was considered at that time that the Commerce Department might be a good alternative as a place to put the trade negotiating functions. This was rejected strongly by the Congress as an inappropriate solution. The Commerce Department represents industry. As a political matter, it cannot negotiate for U.S. agricultural interests, nor is organized labor at all comfortable with the thought that a department that is close to multinational corporations would be their trade representative.

Thus, the idea of the STR, with whose history you are already familiar. The objective was to have the United States represented with a single voice for all of its trade interests: industrial, agricultural, as well as labor; representative of both the Congress and the President, and close enough to the President to be able to judge what is in the political best interests of the Administration and be able to coordinate all of the line agencies that are engaged in trade policy.

The system has worked reasonably well. The question now is how best to strengthen our trade policy coordination, and our enforcement of our rights under the new international agreements negotiated in the MTN; to enforce in the best possible way our unfair trade practice statutes; to organize in a better fashion to promote exports; and to better understand our industrial and trade problems.

In my view, the best answer to this series of questions is to increase the resources given to the trade area and consolidate many of them in a single agency that is not tied to industry, agriculture or labor. Were I still to remain at STR I would never suggest this to you, because it calls in part for an enhancement of the STR function (as well as a strengthening of Commerce's ability to analyze problems and promote exports). Frankly, the STR role has worked well in the past. It is just that the resources are so thin that they are really inadequate to the job that lies ahead.

I have no doubt whatsoever on the basis of cost-benefit analysis that some additional resources in the trade area would pay for themselves many times over. We are opening up \$20 billion of government procurement abroad that has never been open before, but this could have relatively little meaning, in fact, we may lose these benefits, unless we have the people within the U.S. Government to monitor the conduct of others under the Code and assure that our firms can bid abroad. This is perhaps the most dramatic example of the need for strong implementation of our MTN agreements. But we must also actively guard against unfair trade practices under the codes on product standards, subsidies, customs valuation and aircraft, if these agreements are to be of value to us. There are literally billions of dollars of U.S. trade that can hang in the balance depending on how well we enforce these agreements.

I must confess that I am not an expert on government organization. In fact, I have been trying to avoid getting into any interagency dispute on how to carve up trade functions. What I do have a feeling for is the politics of the situation and I know that trade is one of the most political subjects that this Administration or any Administration has to handle.

It makes no difference whether the concerns earlier expressed in this memorandum with respect to the various agencies, constituencies and groups are correct. The paranoia exists in the Congress, the agencies, and in the private sector. It is a fact of life and we have to live with it. The farmers and the unions as well as the manufacturing companies and the importers and the consumers have to feel that their interests are being dealt with fairly. That takes a special combination of political balance and resources that can best be combined in a President's Special Trade Representative, heading a lean trade agency, and remains short of creating a new department.

I would still strongly recommend that you put off a decision at this point. I believe that checking boxes on the OMB memo at this stage would just unleash a storm of controversy that would impair chances for quick approval of the MTN package. I would bring to your attention the fact that some of the options in the OMB memo would have the effect of ending the function of the Special Trade Representative. If this is to be done, it ought to be done on the basis of very serious consideration and consultation with key members of the Congress.

I think this memorandum at this late date is particularly unfair to Jim McIntyre and his colleagues. I have had every opportunity to participate more fully than I have, but the simple truth of the matter is that I always seem to have been juggling a couple of other balls in the air and have been unable to spend any reasonable time on the subject. As a matter of fact this memorandum is being dictated far too hastily and with insufficient thought, which I regret.

cc: Jim McIntyre
Stu Eizenstat

EIZENSTAT
COMMENT

THE WHITE HOUSE

WASHINGTON

May 11, 1979

MEMORANDUM FOR: THE PRESIDENT

FROM: STU EIZENSTAT *Stu*
HOWARD GRUENSPECHT

SUBJECT: Trade Reorganization

The OMB trade reorganization memo reflects a fairly general interagency consensus in favor of greater centralization of export programs and some improvements in the policy coordination process and against realignment of import relief and international negotiation functions. I believe this consensus judgment is basically correct. To go beyond export reorganization would not improve, and could impair, the conduct and substance of our trade and international economic policy.

In order to provide an analytical framework for your decisions on this issue, this memo outlines my objections to the radical reorganization approach of centralizing all trade and international economic functions either into a new Department (Ribicoff-Roth) or into the existing Commerce Department. It also describes how I think we should proceed on the Hill.

The radical reorganization approach would gather substantially all the import relief, export promotion, export regulation, international economic negotiations, and international economic policymaking of the Government into one essentially business-oriented Department. The stated rationale is that this would provide better coordination of U.S. policies relating to international trade and investment.

1. In my view, the argument for trade reorganization along these lines rests on a number of faulty premises:

(a) The most important is the confusion between policy and structure. Trade reorganization will not eliminate conflicts between trade objectives and other U.S. objectives such as budgetary restraint, fighting inflation, affirming American values in our international relationships, etc. Having to choose among conflicting objectives in specific cases is the essence of policymaking and the centralization of functions in a single Department would neither eliminate the inherent conflicts

nor ensure better decisions. In fact, as discussed below, much of the pressure for trade reorganization comes from those who, at bottom, do not object to the organizational framework under which this Administration makes its international economic decisions, but with the decisions themselves.

(b) Centralization of international economic functions in a new Department or in the Commerce Department is unlikely to achieve any significant cost or personnel efficiencies. Those agencies that lose functions and personnel (Treasury, State, and Agriculture) will continue to be involved in the formulation and execution of trade policy and will therefore continue to need trade and international economic staffing capability.

(c) Trade policy has in fact not suffered from lack of coordination. Our MTN performance is a good example of a massive and complex project, involving substantial interagency effort, which was very effectively coordinated. Again, the criticism here is rooted not so much in a feeling that the policies are poorly coordinated but rather in the desire to have the policies themselves changed.

(d) There is no logical reason why responsibility for import relief and export promotion should be housed in the same agency. The opportunities for trade-offs are minimal (e.g., we should not, and legally cannot, deny import relief if genuinely warranted as a trade-off for concessions on exports). Furthermore, the constituencies are very different: export promotion is essentially a single constituency (the business community) issue; import relief involves business, labor, and consumers.

2. It is important to consider the policy biases that a centralized Trade Department might be expected to have. In my view, the orientation would be toward greater protectionism on the one hand and exports as a priority over all other policy objectives on the other. This likely result can be seen from the political pressures and interests that support major trade reorganization:

(a) Much of the pressure on the import side comes from those who basically want a more protectionist (and hence inflationary) trade policy and believe that the concentration of import policy in one constituency-oriented department could further that objective. The problem

with that is that the major economic problem we are likely to face for years to come is chronic inflation. I think that this country simply cannot afford any more inflationary biases in our policymaking machinery, and I would recommend strongly against any reorganization of our import policy functions.

(b) Much of the pressure on the export side comes from companies which have a vested interest in exports and believe that exports should be given a priority over many of this Administration's (economic and other) policy objectives. A good part of the export community would prefer not to have to worry about antiboycott or anti-bribery laws or the effect that human rights, arms restraint, and nuclear non-proliferation policies might occasionally have on exports. They would also prefer greater tax and spending subsidies for exports.

As you can see, these pressures relate not to organizational structure but to differences over Presidential policy. I believe that our policies in these areas have been right -- although we do need to publicize them much better. I think we have fairly balanced our concern for exports with other important objectives. I see no reason to make organizational changes which will bias future policy decisions. The necessary improvement in the operation of our export promotion efforts can be achieved through the more focused organizational measures set out in Section I of the OMB memo without changing the basic thrust of our policies.

3. A radical reorganization would not have any material impact in reducing the U.S. trade or current account deficit (which we expect to be significantly lower this year in any case). As we learned in the export policy study, our balance of payments position depends not on gimmicks but on fundamental economic forces such as international exchange rates, relative growth and inflation rates, and oil imports. However, radical reorganization would raise expectations of dramatic improvement and would therefore increase pressure for policy changes and additional resources when improvement did not follow from organizational change itself. Although we are always re-examining our policies and resource priorities, we should not go out of our way to create expectations that we may not be prepared to fulfill.

4. On the political side of this issue, it appears that the support for radical trade reorganization is rather narrowly based. There is apparently considerable support in the Senate Finance Committee for the Ribicoff-Roth bill but it is unclear how deep that support is since the bill has yet to be subjected to any serious criticism. The bill appears to have little

support in the House. None of the basic Democratic Party constituencies support major trade reorganization. Organized labor, and probably consumer interests as well, would not favor a major transfer of trade functions either into a new Department or into the Commerce Department. Organized labor, which has been fairly quiet thus far on the MTN, could give us major problems if we proposed centralizing a broad range of trade functions in the Commerce Department.

Recommendations

While radical reorganization would be a serious policy error, I believe that export reorganization measures could be both substantively and politically a useful adjunct to the MTN. I recognize that this may not fully satisfy Ribicoff and other advocates of radical reorganization and could make it more difficult to win their support for some of our other proposals. However, the reality of the situation is that Ribicoff's trade reorganization bill or anything similar could do more damage to our country's interests and policies than we can afford.

I recommend that we proceed as follows:

1. In terms of our public position, we should not announce your decisions if Bob Strauss continues to believe that this would damage our chances of winning the MTN. If Bob can get Ribicoff to relent on requiring an immediate announcement as a quid pro quo for DNR, we will not have to join this issue publicly until the MTN legislation has passed Congress. However, any arrangement with Ribicoff must be based on the conditions that: (i) the arrangement creates no explicit or implicit obligation on our part to alter any of your decisions; and (ii) Ribicoff fully understands that we cannot support his concept of trade reorganization and will not reverse any of your decisions under pressure during the MTN debate.
2. Your decisions should be communicated to Ribicoff and perhaps other key Congressmen privately by Jim McIntyre, Bob Strauss and Mike Blumenthal. I think that in quiet, reasoned discussion, Jim, Mike and Bob will be able to make a convincing case that radical trade reorganization would not be in the national interest, and that the organizational and other steps we propose are better focused to achieve our mutually held objectives.

My position on each individual decision has been incorporated into the OMB memorandum.