Keynote Address

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Thank you Chairman Evans and President Singletary. It's a real pleasure to be here today for more reasons than one. First, I should say that it's a real pleasure to be here to hear that introduction. This is the first time I've heard that, and I guess moving people around in the information office has shown a little bit of progress, hasn't it. It's also a pleasure to be here in Kentucky to be with you at your second Energy Conference. I was remarking to Dr. Singletary a little bit earlier, and I noted that this is a subject I do not believe has been receiving, up until now, all the attention that it really deserves. It is certainly my opinion that the field of both energy and environment are the two major issues confronting people today, and energy is just now starting to get the recognition that it deserves, in my opinion. The fact that the University of Kentucky has been in this for some time does show the foresight that is here. It is also a pleasure to be here because my boss happens to come from Kentucky--he's a very proud Kentucky boy. When Roger Morton said, "What are you doing on this date," I said, "Well, really truly, Mr. Secretary, I've been planning on being in Puerto Rico then." He said, "You know that's my home state, and I kind of like it. I think that you would find it very fine in Kentucky on this date," and, I say it's a real pleasure to be here. Well, it is truly a real pleasure to be here to participate in these discussions on energy resources and to supply, I hope, some observations and insights as to the role of government in assuring that energy be available in the forms and quantity required by our growing needs. Now, my contribution will be limited to a point of view. A perspective of how things look from the public sector, of the problems we foresee and some of the thoughts of how we may realize the objective of an adequate, reliable source of energy in the forms we shall need over the next decade or so.

Let me warm up with some large number exercises. No matter what long term growth pattern there turns out to be, the immediate prospect, which is the focus of our attention today, is for our economy to go high-balling along at an annual growth rate of 4% throughout the remainder of this decade and well into the next. We have a trillion dollar per year economy, oriented to serve the needs of 208 million people and by the most conservative, plausible estimates, we shall be 238 million by 1985. We have an enormous restoration job on our hands to rehabilitate our cities and make restitution for the violence we have done in the past to our land, water, and air. We have a commitment to 20 million young people who will be seeking employment during the next decade and we are dedicated to bettering the circumstances of 30 million poor. We are, in short, loaded with obligations which can only be met by continued economic growth over the foreseeable future and, by direct implication, continued increases in the uses of energy at about the same rate. This means roughly a doubling of energy consumption between 1970 and 1985. If we are lucky, coal in its solid form, uranium and hydro-power will provide us with maybe a third of the energy we require in 1985. The other two-thirds will have to be made available in liquid and gaseous forms.

This is the core of our problem. We do not have the capacity to produce energy in these particular forms in the amount we clearly foresee will be needed. If we could get it, we believe we would use 38 trillion cubic feet of gas in 1985. Except for the once-in a-life-time Hugueten discovery, we have never found anywhere near that amount of gas in any single year in our history. The average of the ten best discovery years we have had in the past half century, and this includes Prudhoe Bay, comes to 20 trillion cubic feet--barely more than half of the demanded figure projected in 1985.

Gas is already short, and domestic deliveries are expected to peak out in the next year or so at something under 25 trillion cubic feet annually. Obviously, supplying a demand for 38 trillion cubic feet of gas annually, is an impossible dream. But the energy requirement represented by that figure is no dream -- it's real. What will happen, of course, is that the consumers who can't get their first choice of gas will have to take substitutes -- oil, mainly. We believe that this referred demand to would-be gas consumers may, by 1985, account for as much as 6 million barrels a day of additional oil requirement over and above normal demand for fuels in the liquid form.

We can get the oil on the world market, but only at the price of becoming the captive customer of a notably unstable cartel of oil exporting nations. We would, in such case, end up importing oil to the extent of 58% of our total supply -- 12 million barrels a day of it arriving from the Eastern hemisphere. This is 9,000 ship loads a year of the largest tankers that can now enter the Atlantic sea coast and Gulf ports. Let me be more specific about it. The requirement for liquid and gaseous fuels in 1985 is 87 quadrillion BTU's. Unless there is a dramatic improvement in discoveries beginning this year, we expect to be able to supply less than half of that -- 42 quadrillion BTU's, from conventional indigenous sources of gas. The deficit to be filled by imports of domestically made synthetic fuels is therefore 45 quadrillion BTU's. This is just about equal to the total BTU content of our total oil and gas production in 1971 when we produced 4 billion barrels of oil and 22 trillion cubic feet of gas, and were approaching capacity in both.

This is merely one set of estimates out of many currently being made, and while all prognostications of this sort differ in degree, they all tell the same story -- mainly that our demands for energy, particularly liquid and gaseous energy, are going to be enormous over the foreseeable future and will far outrun the domestic supply base of conventional oil and gas. From this brief sketch of the nature and size of our energy supply problem of liquid and gaseous fuels, I would like to make three observations.

First, we need to regard the various new fuel resources as supplements, not as alternatives, or substitutes, or competitors of the respective conventional domestic fuels. There is no prospect whatever that any one of them could begin to fill the energy gap we foresee over the next fifteen years. The only fuel we will displace will be imported oil, and this only by arrangement with the Federal Government, about which I shall have more to say later.

In this connection I would like to discuss a corollary to this notion that we shall need all the fuels we can get from whatever source, and that no one source can be considered as a true alternative to any other. The corollary is that we shall have to conserve all the energy we can, but that energy conservation can never, by the remotest connection, be considered as an alternative to any measure designed to increase energy supplies. I stress this point because a fallacious argument has been put forth, from some quarters, that if we cut back on our energy usage, we can then defer or avoid developing some of our domestic energy sources such as the oil and gas of the continental shelf or the Alaska north slope, the gasification of coal, or the development of our oil shale resources. This argument is totally without substance or merit, for the relationship between energy conservation and energy production is not an either-or basis. The implacable requirement facing us is for both.

The truth is, we have no choice. We are bound by the harshest necessity both to conserve energy and to produce it in every practicable way of which we are capable. Energy conservation is not an alternative to energy production, and never will be. Our position is similar to that of a man who has happily been living it up on his inheritance until the trustee tells him he is going to go broke in six months. It's quite in order for him to save where ever he can, but he'd better get out and go to work too, or all his savings in the world won't keep him from starving to death when he runs out.

My second observation is that we have got to think big in the proposals we make to restore our position in liquid and gaseous fuels. The supply problems we face are huge, and the solutions we address to them must be the same order of magnitude. Item: a shale oil mining and processing installation of commercial size will give us 250 thousand barrels a day of synthetic fuel oil. Time: the early eighties. It would take maybe three years to build it and get it operating at designed capacity. In those three years the gap between our liquid fuel requirements and our domestic supply will have increased by 3 million barrels a day, giving the effect of both rising demand and falling productive capacity. Item: a 250 million cubic foot per day plant to make pipeline gas out of coal, again in the early 80's -- three years and 250 million dollars later it is doing its thing. But if we haven't built thirty more plants the same size or greater during the same time period, we shall be worse off for gas supply at the time it goes on stream than we were when we began construction. Always there will be this relentless upward tug on the demand line and, as the Red Queen said to Alice, "We shall have to run twice as hard just to stay in the same place".

My third point is that government participation is critical to the success of the efforts made by private industry to provide these new sources of energy. On various platforms around the country I have repeatedly made two points about the relationship between government and industry. The first is that as a general rule, the more government gets involved with energy problems, the more difficult and intractible the problems become. The second is that government is inevitably going to become much more heavily involved in energy demands in the future tha it ever was in the past. The conjunction of these two opposite premises in the same argument has come to be known as "Dole's Dilemma". That is, how to manage the necessary participation of government, particular the Federal Government in what is essentiall a private endeavor, and do it in such a way that the private sector can still do its job effectively.

In the time remaining me, I would like to discuss certain aspects of government participation in the ventures identified wit bringing new sources of energy on line. The first of these is government attitude and policy toward imported forms of energy.

The oil import program that we have in effect since 1959 is in the process of shifting gears. Until this year, the progra was administered to accomodate a surplus in productive capacity east of the Rocky Mountains. The surplus has now disappeared, and the oil industry throughout the United State is producing virtually at capacity. The new emphasis on the program will be to permit imports to fill the gap between demand and production, both east and west of the Rockie But make no mistake about it, the policy is still to restrict imports, and this has got to be continued to be our policy if we are ever to see the commercial development of synthetic fuels from domestic oil shale and coal. The reason for this is quite apparent if we invision any escape from a steadily increasing dependence upon foreign sources for our energy, our policy must not only encourage the development of domestic energy sources, but it must manage the problem of imports in a way that affords a reliable, long-range planning basis for the domestic energy industries.

This is particularly important for the clean synthetic fuels that we obtain from coal and oil shale. It will take us at least 15 years to acquire a significant capability to produce oil and gas from coal and oil shale. This will require large amounts of capital beginning now, and continuing each year in rising volume. This capital must be provided, by and large, by the private sector which must reconcile its investment with a sizeable difference between its cost of producing these commodities and the laid-down price of foreign oil. It will recognize, too, that while the price of foreign oil has risen sharply, and may continue to rise in the future, the cost of this oil to the producing countries themselves has risen hardly at all. If we give them open entry to the U.S. market, the oil exporting nations could, with the proper pricing strategy, keep large scale investment in domestic synthetic fuel permanently on the shelf. My point is that while we have vast energy resources available to us in our own ground, our policy toward developing those resources is inseparable from our policy toward oil entering our markets from abroad.

In a political year it is natural to expect that certain policy areas should bear a strong flavor of politics, and 1972 is certainly no exception. The tax treatment enjoyed by the natural resource industries has long been subject to attack by those who make the assumption that the advantages occurring from those tax provisions are carried down, in tact, to the bottom line of the profit and loss statement of the companies taking those deductions. It has recently been given added visibility under the guise of tax reform.

Let's review some elementary economics. Taxes, like any other cost element, are a determinant of both price and return on investment. Any change in cost, up or down, will effect either price or rate of return -- and usually both. Any increase in taxes that cannot be offset by reduction in costs elsewhere, must be recovered in increased price of the product, or rate of return on investment will decline. A decline in rate of return on investment is inevitably going to be followed by a decline in investments. That is to say, a decline in the renewal and expansion of properties that produced goods and services. Just as inevitably, this decline in investment will be followed by a decline in availability of the product it supplies, and we have the clearest kind of evidence for that in the gas industry.

A decline in the availability of product, unless countered by reduced demand, means higher prices. Who pays? The consumer -- that's who. The consumer of oil and gas, and that means just about everybody in the United States, will eventually pick up the whole tab for any cost increases to the petroleum industry resulting from the phase out of depletion allowances for oil and gas. He will pay in higher prices, in inconvenience, in narrow range of choice and, quite conceivably, in the simple unavailability of the products he wants and needs. This is the meaning and consequence of any proposals to phase out depletional allowances that have historically been a part of the tax structure of the mineral industries.

Those who make this proposal rationalize the action as posing a loop hole. Unfortunately, this particular loop hole has an embarrassing feature -- the consumer's neck is in it. The point is, that regardless of their form, and how they are collected, costs are costs and they must eventually be paid by the consuming public. This is as true in a communist society as it is in our own and no amount of manipulation and legerdemain can do more than shift the costs from one place to another, or from one time to another. But once incurred, it never goes away. No matter how closely you try to control market for something it always remains a free market in this important sense. In the end, you get only what you pay for, and if you don't pay enough, you don't get enough.

Our policy toward natural gas pricing at the well head is a classic illustration of how we traded adequacy in the security of supply for the objective of low cost, and were rewarded by having to pay higher prices anyway. The arithmetic of costs, prices, and the return to investment is only one feature of the producer's decision making process. The fundamental requirement for minerals exploration and development is access to areas where mineral deposits might reasonably be expected to occur.

It happens that most of the mineralized lands in this country lie in the public domain, so that the obligation to provide access is a particular concern of the Federal Government. In his clean air message of June 4, 1971, President Nixon specifically gave his endorsement to measures aimed at developing the energy resources of the Federal lands. Of the options available, the oil and gas resources of the outer continental shelf promise the earliest, largest, and cheapest increments to the nations supply of domestic liquid and gaseous fuels that are available in the lower 48 states. Recognizing the great potential of the outer continental shelf, the President directed the Secretary of the Interior to expand and accelerate the leasing of OCS lands for oil and gas exploration. Secretary Morton responded with a five year program calling for at least two general sales through 1975. The first of these sales, comprising some 366 thousand acres of land east of Louisiana was originally scheduled for December of 1971. It was voided by a court order resulting from a suit brought by three environmentalist groups charging that the requirements of the NEPA (National Environmental Protection Act) had not been met.

The other sale, offering approximately the same tracts, was allowed to take place last month. It brought nearly 600 million dollars in bonuses for the highest average per acre on any general lease sale ever held by the Federal Government -- a measure of how desperate producers are for the prospective acreage. I might add that on October 12, 1972, just a few days ago, 11 permits to drill had been applied for by the initial

bidders on these tracts.

This delay threw the schedule nine months behind on the particular sale and it has so far caused a delay of seven months in the sale that was originally scheduled to have taken place in May of this year. The proposal for the May sale is now under going the public review process required by the NEPA and we are hopeful that we can obtain the necessary clearance to permit it to take place in December. It is a large sale -- offerings total 135 tracts totaling 618 thousand acres off Louisiana. Thus, between the two sales, approximately one million acres will have been made available for exploration and development of oil and gas reserves. It is my firm hope that we can, in the Department of the Interior, continue to offer at least one million acres in each year here after.

A third sale originally scheduled for November of 1972 has, in consequence of the other two delays, been pushed over into 1973, tentatively considered for sometime this spring. This will be an offering of tracts off east Texas, in what is generally conceded to be a gas prone territory. A list of 116 tracts has been made available for public inspection and work is underway on the Draft Environmental Impact Statement which will be issued prior to public hearing in accordance with the NEPA. The delays and difficulties we have experienced in obtaining approval for these lease sales are, of course, characteristic of minerals development these days. Whether the focus of concern be a pipeline in Alaska, a drilling platform in the Santa Barbara channel or a strip mine here in Kentucky, the fact is that the historic national policy of mineral access, which for more than a century has provided a basis for our phenomenal prosperity and growth, is being upset by the politics of a newly organized concern -- environmentalism.

The advent of a public policy which required due attention to the environment, which restricts needless destruction of life systems and demands that development of natural resources proceed with the minimum practical interference to other uses that may be made of the land, can only be applauded by any thinking citizen. It's great -- it's wonderful, and we all ought to be for it. But this is not the issue. The issue which is developing, is that of total denial of access to extensive areas where mineral operations are entirely feasible within all reasonable requirements for environmental protection. Thus, we have proposals put forth which aim, not at the regulation of strip mining and the correction of its abuse, but at abolishing it all together. There was at least one bill that expired with the 92nd Congress that would have accomplished this within six months of its passage. Fortunately this particular piece of legislative lunnacy got nowhere. But the very fact that such insanity could be dignified as a serious proposal to the National Legislature, or that a candidate for the nations' highest office could give it his unqualified endorsement, bespeaks the presence of a mood within the body politics which should be a matter of profound concern to us all.

I know from the program that the synthetic fuels are to be discussed at length in the session on inter-fuel conversion this afternoon and my comment on them here will address only what I perceive to be the gover ment-industry relations involved. As I have already intimated, the creation of synthetic fuels in the industries will require enormous outlays of capital, scientific and tech nological know-how and managerial expertise. It will be difficult to find a single compan with access to these resources in the magnitude that will be required. A cooperative effort between the private and public sector representing a pooling of money, and talent, and innovative ideas is essential to launch these ventures on the scale which the gravit of the energy situation demands.

As President Nixon has noted in his message on the new technology initiatives, and I quote, "We must appreciate that the progress that we seek requires a new partner ship in science and technology -- one which brings together the Federal Government, private enterprise, state and local government and our universities and research centers in a coordinated cooperative effort to serve the national interest". We are not used to doing this, except under the stress of emergency conditions, and minimal obstacl to such a fusion of capital, effort and information exists in both custom and law. Th access to, and equitable use of capital information is involved, as the propinquity of companies in a competitive situation against each other. The whole process by which the Federal Government procedures research development services deserves a fair going review. President Nixon has taken not of these obstacles and has requested funds to enable the National Science Foundation to study these barriers to technological innovation, and consequences of alternative Federal policies which would reduce or eliminate them.

No matter where we look, the role of government as an agent in the energy supply and demand process is always there. The program I have sketched this morning only glimpses here and there, the many influence which form the milieu for the actions and policies with regard to energy. All interact, one with the other, and upon the avail ability of energy supply. All should have far more attention than they have so far been given under an administrative mechanis that would, again in President Nixon's word and I quote, "... provide a focal point whe energy policy in the executive branch could be harmonized and rationalized". The Presi dent's proposal to reorganize the executive branch, which includes the location of a Federal Government responsibility for energ matters in an energy and mineral resources administration within a new department of Natural Resources has been given short trip by the 92nd Congress -- this despite the support of many of the outstanding leaders of both parties. But ignoring a proper solution does not make the problem go away. It will still be around when the next Congress convenes and undoubtedly the request

for legislative action on the present proposal will be renewed. Nothing will have changed except, hopefully, the disposition of the Congress. At that time I hope that all of you will see fit to lend your active support to this needed and worthwhile objective.

It has been a pleasure to be with you and I extend my every good wish for our productive meeting on what I consider the most timely and important subject that is facing this country today. My best wishes and thanks for being here.