FOREIGN OIL AND TAXATION: THE NEED FOR A COORDINATED ENERGY POLICY

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I. Introduction

The United States has lacked a coordinated energy policy since the beginning of the energy crisis decade of the 1970's. The primary focus of policy-makers has been United States dependence on foreign oil,[1] but no consistent policy towards it has been developed. At the height of the OPEC oil embargo, 1973 to 1974, President Nixon announced that the United States would never be dependent on foreign oil again nor be held hostage by OPEC. Project Independence was aimed at achieving energy self-sufficiency by 1980.[2] However, Project Independence produced only a lengthy document having few readers.[3] The long gas lines were temporary inconveniences.

The situation returned to near normal until the energy crisis became the "moral equivalent of war" under the Carter administration.[4] President Carter's approach to the problem of dependence on foreign oil was conservation[5] as a panacea. An impending national catastrophe was to be averted by conservation of the world's scarce petroleum reserves.[6] Nevertheless, consumers continued to buy oil and gas despite the continued rise in the price of foreign oil. Today, warnings of scarcity go unheeded after being heralded so often.

Many projects have been abandoned. Exxon Corporation has

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[1] *See* President's Address to the Nation Outlining Steps to Deal with the Emergency, 9 Weekly Comp. Pres. Doc. 1312-18 (Nov. 7, 1973); President's Message to Congress, 9 Weekly Comp. Pres. Doc. 1318-22 (Nov. 8, 1973); President's Report to the American People, 13 Weekly Comp. Pres. Doc. 138 (Feb. 2, 1977); and President's Address to the Nation, 13 Weekly Comp. Pres. Doc. 560-65 (Apr. 18, 1977).

[2] Speech to the Nation, 9 Weekly Comp. Pres. Doc. 1312, 1317 (Nov. 7, 1973).

[3] Federal Energy Administration, Project Independence (1974), hearings were held in ten major United States cities and more than ten volumes were compiled.

[4] Address to the Nation, 13 Weekly Comp. Pres. Doc. 560, 561 (Apr. 18, 1977).

[5] *Id.* at 563-64.

[6] President Carter warned of the impending national catastrophe. *Id.* at 560.

abandoned its multi-million dollar oil shale project.[7] Nuclear power plant construction and operation has been curtailed or suspended.[8] President Reagan has even suggested dismantling of the Department of Energy.[9] There now appears to be a glut of crude oil on the world market[10] and the energy crisis is almost forgotten. However, no comprehensive energy policy has yet been formulated.

Energy policy is a political pawn used to placate the various constituencies in the world and national political arenas. United States policy toward foreign oil could be predicated on one of two extreme positions. First, United States policy could be no policy: to give real effect to the Project Independence posture of making the United States self-sufficient with regard to petroleum products. This policy is manifested in the conservation program; development of alternative forms of energy such as nuclear, solar, wind, hydroelectric, and other fossil fuels; development of synthetic petroleum products; and increased exploration and production of domestic oil reserves. Second, the policy with regard to foreign oil could be to buy as much as possible at whatever price. This alternative posture seems to be one based primarily on national security and foreign policy. The United States must maintain good relations with oil producing countries particularly in the Middle East to stabilize the area and reduce the Soviet influence. Domestic production has peaked[11] so that foreign oil is necessary to maintain modern, oil-dependent technology and machinery which in turn support United States defense capabilities. To accomplish this goal foreign oil purchases are stored in strategic reservoirs for future use rather than for immediate consumption.[12] This practice has strained relations with some oil producing sovereigns who see their future power base being eroded.[13] There is also the baser instinct

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[7] TIME, May 17, 1982, at 58-59.

[8] Since the accident at the nuclear reactor at Three Mile Island, the Bailey Nuclear Plant construction has been abandoned and the Diablo Canyon Reactor in California operation has been delayed. Three Mile Island had a chilling effect on the nuclear power industry. NEWSWEEK, Feb. 8, 1982, at 63 and NEWSWEEK, Apr. 19, 1982, at 101.

[9] *See* Statement of Plan to Dismantle the Department of Energy, 17 WEEKLY COMP. PRES. Doc. 1378 (Dec. 17, 1981).

[10] NEWSWEEK, Mar. 29, 1982, at 64.

[11] *See* President's Address to the Nation, 13 WEEKLY COMP. PRES. DOC., 560, 561 (Apr. 18, 1977). *But see* Statement of M.A. Adelman, petroleum economist, U.S. NEWS & WORLD REP., Apr. 9, 1979, at 22, in which he states that proved plus probable reserves will suffice for 50-100 years depending on the rate of consumption.

[12] *See* Message to Congress Transmitting the Plan, 17 WEEKLY COMP. PRES. DOC. at 772 (July 17, 1981) in which the rapid filling of our strategic petroleum reserves is called for.

[13] If the United States fills its strategic petroleum reserves during the current oil glut,

for survival which dictates that the use of "their" oil first and hoarding "ours" for use after "they" have run dry.

Because of the lack of a coordinated energy policy, United States policy with regard to foreign oil travels the spectrum between the two extreme positions. This article examines the manifestations of this lack of a coordinated policy in the area of taxation.

II. TAX POLICY

A. *Foreign Oil*

Most tax jurisdictions in the world impose taxes on the basis of source of income. In addition, many countries tax on the basis of residence or citizenship. In the United States the federal government uses source,[14] residence,[15] and citizenship[16] as bases of taxation. Consequently, multinational enterprises often are subject to double taxation of the same income; one jurisdiction would tax based on the source of income, and the other jurisdiction on the basis of residence and/or citizenship. Since such double taxation would inhibit exploration and extraction of oil and gas and other minerals abroad, Congress has provided the foreign tax credit in I.R.C. §§ 901-907. The United States, having become the country of residence or citizenship of many multinational enterprises, therefore allows as a credit against its income tax certain taxes paid to the country of source. However, only foreign income, war profits, and excess profits taxes paid or accrued during the taxable year or taxes that are in lieu of those taxes are creditable against the United States income tax.[17] Alternatively, a taxpayer who has paid or accrued creditable foreign taxes may elect to deduct those taxes rather than take them as a foreign tax credit.[18] A taxpayer who elects to take the foreign tax credit may not also elect to deduct foreign taxes for any taxable year that the taxpayer elects to take the tax credit.[19]

Since the purpose of the foreign tax credit is the avoidance of

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OPEC's political weapon, the oil boycott, will not be effective in the short term.

[14] U.S. CONST. amend. XVI, gives Congress the power to tax income "from whatever source derived."

[15] The doctrine of state's sovereignty dictates that the state exercise its legislative power over its own territory and that power extends to all persons within that territory whether a national or alien. *See* Burnet v. Brooks, 288 U.S. 378 (1933).

[16] Cook v. Tait, 265 U.S. 47 (1924).

[17] I.R.C. §§ 901(b)(1), 903 (1976).

[18] I.R.C. § 164(a)(3) (1976).

[19] I.R.C. § 275(a)(4) (1976).

double taxation by two or more sovereigns on the same income, the foreign tax credit is not intended to be used to recharacterize an expense such as royalties as a tax which can then be taken as a foreign tax credit. On November 4, 1950, the Saudi Arabian government issued a Royal Decree which imposed a general income tax on the incomes of individuals and corporations in Saudi Arabia.[20] On December 27, 1950, the Saudi Arabian government imposed an additional tax on every company registered or required to be registered in accordance with the decree for the registration of companies which were engaged in the production of petroleum or other hydrocarbons in the Kingdom of Saudi Arabia.[21] In 1955, the Internal Revenue Service, in Revenue Ruling 55-296,[22] held that both the general income tax and the additional tax imposed by the Saudi Arabian Royal Decrees would be allowed as a credit against United States income tax. Revenue Ruling 55-296 appears to have been politically motivated. In the pre-energy crisis era, United States imports of foreign oil were not critical. Prices were not exorbitant since the major oil companies were dictating prices to the oil producing sovereigns. Moreover, it was beneficial to the major oil companies to have their royalty payments characterized as taxes. The tax construed to be an income tax would be credited against their United States income tax liability. By allowing a tax credit for this type of payment to Saudi Arabia, the United States could be viewed as providing indirect foreign aid to Saudi Arabia by shifting money from the United States treasury to the Saudi Arabian treasury. As a matter of foreign policy, the United States had relinquished a major part of its policy-making responsibility to the major oil producers in the Middle East in order to maintain an American presence and degree of control over the situation in the Middle East. Maintaining an American presence and having American oil companies develop the oil resources in the Middle East were deemed to be more desirable than allowing those oil resources to come under the influence of hostile authority. The problem involved with the foreign tax credit is the dual function of oil producing sovereigns. Not only is the land owned by the sovereign so that the sovereign collects royalties as an ordinary owner of property, but the sovereign also has the power to levy taxes. Although the oil producing sovereigns characterize the payments as taxes,

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[20] Royal Decree No. 17/2/28/3321.

[21] Royal Decree No. 17/2/28/7634.

[22] 1955-1 C.B. 386.

the payments actually have more attributes of royalty payments than taxes.

The Internal Revenue Service subsequently reconsidered its position in Revenue Ruling 55-296 that allowed the credit for both taxes.[23] In Revenue Ruling 78-63 the Service revoked Revenue Ruling 55-296,[24] and determined that the additional tax imposed by the decree of the Saudi Arabian government was not an income tax. The additional tax imposed by decree as computed was based on a posted price established by the Saudi Arabian government. The posted price in most cases exceeded the actual market price; therefore, the tax was not imposed on actual income but on an artificial or ficticious income based on the posted price and, consequently, was noncreditable as an income tax. Like Revenue Ruling 55-296, Revenue Ruling 78-63 also had political overtones: it was issued during the energy crisis of 1977-78.

Revenue Ruling 78-63 is in accord with I.R.C. § 901(f) which provides that certain payments for oil or gas are not considered as taxes if the taxpayer has no economic interest in the oil and gas depleted under I.R.C. § 611(a),[25] and either the purchase or sale is at a price which differs from fair market value. If both conditions are satisfied then the amount of income or war profits or excess profits taxes paid or accrued to any foreign country, in connection with the sale or purchase of oil and gas extracted in that country, is neither a deductible tax under I.R.C. § 275(a)(4) nor a creditable tax under I.R.C. § 901. An economic benefit in oil and gas which is depletable means an ownership interest whereby the owner extracts the mineral in order to gain a return on the capital invested.[26] A person with no capital investment in the mineral deposit does not possess an economic interest merely by deriving an economic or pecuniary advantage from production as a result of a contractual relationship.[27] In order to have a creditable foreign tax where a foreign government owns the minerals being extracted the taxpayer must satisfy five requirements.[28] First, the amount of the

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[23] *See* Rev. Rul. 78-63, 1978-1 C.B. 228.

[24] *Id.* at 232.

[25] Depletion is only allowed to the owner of an economic interest. Depletion may be defined to be the exhaustion of oil and gas reserves by extraction. A deduction is allowed to compensate taxpayers for the diminution of their oil and gas reserves. I.R.C. §§ 611, 612, 613, 613A (1976); Anderson v. Helvering, 310 U.S. 404 (1940).

[26] Treas. Reg. § 1.611-1(b)(1) (1968).

[27] *Id.*

[28] Internal Revenue News Release IR-1638, [1976] 9 STAND. FED. TAX REP. (CCH) ¶ 6751

income tax must be calculated separately and independently of any royalty or other tax paid to the government.[29] Second, under the law and its administration the foreign income tax must be imposed on the receipt of income by the taxpayer using principles consistent with the United States concept of realization, and such income must be determined on an arms length basis.[30] Third, the income tax liability cannot be discharged with property owned by the foreign government; that is, the payment may not be made in kind.[31] Fourth, the income tax liability is to be computed on the basis of results of the taxpayer's entire extractive operation.[32] Fifth, the taxpayer must be allowed to deduct significant expenses incurred in such extraction.[33] Revenue Ruling 78-222 imposes a sixth requirement that the foreign government must require payment of a royalty or other consideration in addition to payment of income tax.[34] Under Temporary Regulation § 4.901-2,[35] a foreign tax is an income tax if and only if the charge is not compensation for a specific economic benefit, the charge is based on net realized income under standards similar to the United States realized income standards, and the charge follows the reasonable rules of the taxing jurisdiction.[36]

On the surface the foreign tax credit appears to be neutral as far as the energy ramifications are concerned and is merely intended to avoid double taxation of foreign source income by a foreign sovereign and the United States. The foreign tax credit ensures that the taxpayer will pay the higher rate of the United States or the foreign country.[37] However, the credit is not intended to provide a

(July 14, 1976).

[29] *Id.*

[30] *Id.*

[31] *Id.*

[32] *Id.*

[33] *Id.*

[34] 1978-1 C.B. 232.

[35] Temporary Treas. Reg. § 4.901-2, [1981] 6 STAND. FED. TAX REP. (CCH) ¶ 4302A (adopted by T.D. 7739, Nov. 12, 1980).

[36] *Id.* § 4.901-2(a)(1)(i) to (iii).

[37] I.R.C. § 907(a) (1976) limits the tax credit on foreign oil and gas extraction taxes for corporations to the highest rate specified in I.R.C. § 11(b) (1976) and in the case of individuals to the effective United States tax rate. Corporations or individuals who paid or accrued foreign oil and gas extraction taxes at a rate equal to or higher than their United States tax rate will pay no United States income tax but will pay the entire amount of foreign oil and gas extraction taxes levied by the foreign sovereign. Corporations or individuals who paid or accrued foreign oil and gas extraction taxes at a rate lower than their United States tax rate will receive a full credit for the foreign oil and gas extraction taxes paid or accrued and pay at the higher United States tax rate.

tax advantage to foreign investors. The amount of the credit is limited to United States tax liability as provided in I.R.C. §§ 904 and 907.[38] The foreign tax credit, however, does encourage foreign investment by eliminating double taxation and provides foreign investment companies with essentially the same tax base that domestic corporations have. Thus, the foreign tax credit provides for a horizontal equity between domestic oil-producing operations and foreign oil-producing operations. By not discriminating against foreign exploration and extraction of oil and gas, the foreign tax credit indirectly encourages foreign exploration and extraction operations. The foreign tax credit also serves United States foreign policy by providing indirect economic aid to friendly foreign sovereigns. It also provides the same aid to less friendly sovereigns. Although the foreign tax credit is not a direct tax expenditure, it is a shifting of tax revenues from the United States treasury to a foreign treasury. Certainly as a matter of energy policy, in the event that the United States desired to curtail or eliminate the influx of foreign oil into the United States, severe limitation or disallowance of the foreign tax credit on foreign oil and gas income would be a logical step in accomplishing that goal.

I.R.C. § 907 provides special rules for the treatment of taxes on foreign oil and gas extraction income[39] and foreign oil related income.[40] Section 907 places limitations on the amount qualifying as foreign taxes for purposes of the foreign tax credit in I.R.C. § 901.

After December 31, 1982, I.R.C. § 907(b) excludes from the term "income, war profits, and excess profits taxes" any foreign tax on foreign oil related income which is "materially greater"[41] than for-

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[38] The limitation in I.R.C. § 907(a) (1976) is discussed in footnote 37, *supra*. I.R.C. § 904 (1976) imposes a limitation on the foreign tax credit to the extent of United States tax before the credit. Section 904 is intended to prevent higher foreign tax rates from being subsidized from the United States treasury through the tax credit.

[39] Foreign oil and gas extraction income is taxable income derived from foreign sources from the extraction of minerals from oil and gas wells by any person or the sale or exchange of those assets used by the taxpayer in the extraction of minerals from oil and gas wells. I.R.C. § 907(c)(1) (1976).

[40] Foreign oil related income is taxable income derived from foreign sources from the processing, transportation, or distribution or sale of minerals from oil or gas wells or primary products or the sale or exchange of assets used by the taxpayer to produce foreign oil related income. I.R.C. § 907(c)(2) (1976).

[41] The term "materially greater" will be defined by the Internal Revenue Service in a future regulation, although the statute provides that "materially greater" will be measured "over a reasonable period of time." Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, § 211(c)(1), 96 Stat. 324 (1982) (enacted Sept. 3, 1982 and codified at I.R.C. § 907(b) (1982)).

eign taxes generally imposed by that sovereign on income that is not foreign oil related income nor foreign oil and gas extraction income.[42] Such excess will not be a creditable tax for purposes of I.R.C. § 901; however, that amount is to be treated as a deduction under the law of the foreign sovereign.[43] The effect of the § 907(a) limitation is to limit the amount of the creditable tax from foreign oil and gas extraction income to that amount which would have resulted if the maximum United States tax rates were used.[44]

Congress also has repealed the separate I.R.C. § 904 credit limitation computation required by I.R.C. § 907(b) for foreign oil related income and other taxable income.[45] The separate limitation on foreign oil related income required by I.R.C. § 907(b) prior to December 31, 1982 provided an additional limitation on the foreign tax credit and worked to the benefit of the federal government where other business activities were taxed at rates lower than the foreign oil and gas extraction tax rate. This change for taxable years beginning after December 31, 1982 is accompanied by a change in the definition of foreign oil related income. Foreign oil and gas extraction income had been included in the definition of foreign oil related income. Since foreign oil and gas extraction tax credits were limited by I.R.C. § 907(a), foreign oil related income was treated separately in computing the creditable tax under I.R.C. § 901. Foreign oil and gas extraction income has been removed from the definition of foreign oil related income[46] by the repeal of the separate computation requirement. I.R.C. § 907 is designed to prevent a taxpayer from using foreign tax credits which would reduce United States tax liability upon United States source income.[47] Any excess foreign oil and gas extraction income taxes which are not allowed as a tax credit because of limitations in I.R.C. § 907 are not deductible.[48] The limitations in I.R.C. § 907 discourage oil companies from production of foreign oil and gas in those countries where the extraction taxes exceed the maximum

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[42] *Id.*

[43] *Id.*

[44] *See supra* note 37.

[45] *Id.* The repeal of the § 904 credit limitation is effective for taxable years beginning after December 31, 1982.

[46] Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, § 211(b), 96 Stat. 324 (1982) (enacted Sept. 3, 1982 and codified at I.R.C. § 907(c)(2) (1982)).

[47] H.R. REP. No. 94-658, 94th Cong., 2d Sess. 223 *reprinted in* 1976 U.S. CODE CONG. & AD. NEWS 2897, 3653-54.

[48] I.R.C. § 275(a)(4) (1976).

tax rate imposed on such income in the United States. No incentive is provided to produce foreign oil and gas to the exclusion of domestic oil and gas production, because the excess foreign oil and gas extraction taxes cannot be used to offset United States income tax of domestic oil and gas production income. Moreover, the excess foreign oil and gas extraction income tax may not be deducted under I.R.C. § 275(a)(4); therefore, the tax benefit ceases except for the carryover provisions which are also limited.

The two percent of foreign oil and gas extraction income limitation on the carryback or carryover of excess foreign oil and gas extraction income taxes not creditable in a taxable year has been repealed.[49] After December 31, 1982, the excess of any foreign oil and gas extraction taxes not allowed as a tax credit in a taxable year may be carried back two years or forward five years provided that the excess carryback or carryover, plus other creditable taxes, do not exceed the I.R.C. §§ 904 and 907(a) limitations. These tax credit limitations also serve as a deterrent to a foreign oil and gas producing sovereign from imposing high tax rates on foreign oil and gas extraction income. Since the foreign tax cannot be credited against United States income tax, oil producing enterprises subject to United States income tax would curtail activities in any country imposing a higher tax rate because there would be no corresponding tax benefit for the high foreign oil and gas extraction income tax rates. From a policy standpoint, the limitations on the foreign tax credit allowed under I.R.C. § 901 only deter production of oil and gas in those countries in which the foreign oil and gas extraction income taxes exceed the United States tax rate. Those limitations, however, do not discourage foreign oil and gas production in those countries in which the foreign oil and gas extraction income tax is equal to or less than the tax rate imposed by the United States.

In retrospect, United States tax policy with regard to the foreign tax credit in the past has encouraged production of foreign oil and gas, as evidenced by the early lenient view of the Internal Revenue Service in treating disguised royalty payments as taxes and allowing those payments to be credited against United States income tax. As the political situation in the Middle East deteriorated and OPEC gained power, United States policy toward the foreign tax credit began to change. First, the I.R.S. reassessed its earlier views

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[49] Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, § 211(d)(2), 96 Stat. 324 (1982) (enacted Sept. 3, 1982 and codified at I.R.C. § 907(f) (1982)).

with respect to the disguised royalty payments and declared that those payments were no longer creditable.[50] In the Tax Reduction Act of 1975,[51] the Tax Reform Act of 1976,[52] and the Tax Equity and Fiscal Responsibility Act of 1982,[53] Congress imposed limitations on the foreign tax credit allowed for foreign oil and gas extraction income taxes and foreign oil related income taxes so that the maximum foreign tax credit on foreign oil and gas extraction income taxes would be no more than the tax that would have been imposed on United States source income. The result is that the foreign tax credit provides some incentive to continue foreign oil and gas production but only in those countries where the foreign oil and gas extraction income tax rates do not exceed the maximum United States income tax rate that would be imposed if it were United States source income.

B. *Domestic Oil*

As a matter of energy policy if one is to curtail the importation of foreign oil, provisions must be made for the replacement or substitution of that foreign oil supply. Substitution of the foreign oil supply requires encouragement or incentives to increase domestic exploration and production, the development of synthetic fuels, development of solar, wind, hydroelectric sources, or the development of other fossil fuels. United States tax policy affects the development of these alternative sources.

Two primary parts of President Carter's energy policy were the Crude Oil Windfall Tax Act of 1980[54] and the phased decontrol of domestic crude oil prices.[55] The price controls on domestic crude oil production were originally established in 1971 and modified in 1973 and 1976.[56] Then, in April of 1979, President Carter an-

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[50] *See supra* notes 23-24 and accompanying text.

[51] Pub. L. No. 94-12, 89 Stat. 26 (1975).

[52] Pub. L. No. 94-455, 90 Stat. 1520 (1976).

[53] Pub. L. No. 97-248, 96 Stat. 324 (1982).

[54] Pub. L. No. 96-223, 94 Stat. 229 (1980). A Windfall Profits Tax had been previously proposed by President Nixon in President's Message to the Congress Outlining Legislative Proposals and Executive Actions to Deal with the Crisis, 10 WEEKLY COMP. PRES. Doc. 72-3, 76-7 (Jan. 23, 1974).

[55] For President Carter's presentation of this program in a Message to Congress, *see* 15 WEEKLY COMP. PRES. Doc. 721-27 (Apr. 26, 1979).

[56] The price controls were adopted pursuant to the Economic Stabilization Act of 1971, Pub. L. No. 92-201, 85 Stat. 743 (1971). The 1973 price controls are found in 38 Fed. Reg. 33,577 (1973). In 1976, the Energy Policy and Conservation Act, Pub. L. No. 94-163, 89 Stat. 871 (1975), was enacted and new domestic crude oil price regulations were adopted in 41

nounced a program to phase out these price controls by October 1, 1981.[57] The windfall profits tax was designed to be a substitute for price controls. Economically, the difference was that the prices would be controlled at a higher level. The windfall profits tax is an excise tax on the selling price of crude oil.[58] The tax is imposed on excess of the selling price over the base price.[59] Generally, the windfall profits tax is similar to a state severance tax. The windfall profits tax is imposed upon producers of all domestic crude oil removed from property on or after March 1980 with certain exceptions.[60] The reason for decontrol of the 1971 price restrictions was to stimulate domestic exploration and production of crude oil and gas. However, deregulation coupled with the windfall profits tax has the opposite effect. The incentive to increase domestic exploration and production of crude oil and gas is dampened by the imposition of the windfall profits tax which merely raises the controlled price that producers may receive for the product. One of the justifications of the windfall profits tax, which is designed to aggregate a net of 227.3 billion dollars in windfall profit tax revenues,[61] was a reallocation of resources from oil to alternative energy sources. The windfall profits tax revenue was designed to support research and development in other energy areas.[62] Thus, the tax was imposed as part of a coordinated energy policy. The coordinated energy policy appeared to be a simultaneous reduction of foreign oil imports and an increase in the availability of other domestic energy supplies, not necessarily crude oil, the production of which was believed to have peaked in the United States.[63] Other tax legislation was enacted primarily to conserve oil and gas.[64]

Fed. Reg. 4931 (1976).

[57] 15 WEEKLY COMP. PRES. DOC. 721-27 (Apr. 26, 1979); 44 Fed. Reg. 22,010 (1979).

[58] I.R.C. § 4986(a) (Supp. V 1981).

[59] I.R.C. §§ 4988, 4989 (Supp. V 1981).

[60] *See* I.R.C. § 4994 (Supp. V 1981) for exceptions.

[61] I.R.C. § 4990(d)(2) (Supp. V 1981). The Crude Oil Windfall Profits Tax will be phased out by the later of December 1987 or the first month after December 1987, but before December 1990 in which an aggregate of $227.3 billion is reached.

[62] An Energy Security Fund was designed to be the conduit through which revenues from the windfall profits tax were to be channeled to support better design and efficiency of automobiles and appliances, mass transit systems, and research and development of other fossil fuels, oil shale, synthetic petroleum, solar, wind, and hydroelectric energy sources. *See* Address to the Nation, 15 WEEKLY COMP. PRES. DOC. 609-14 (Apr. 5, 1979) and Message to the Congress, 15 WEEKLY COMP. PRES. DOC. 721-27 (Apr. 26, 1979).

[63] *See supra* note 11.

[64] *E.g.*, Energy Tax Act of 1978, Pub. L. No. 95-618, 92 Stat. 3174 (1978). I.R.C. § 44C (Supp. V 1981) was added to the Internal Revenue Code to provide a tax credit for residen-

In retrospect the Carter energy program seems to have been the most comprehensive of the energy programs to date although parts of it were working at cross purposes.

III. OIL IMPORT FEE

If United States energy policy is to curtail the importation of oil and gas and thereby reduce American dependence on foreign oil, an oil import fee could be imposed on each barrel of foreign oil imported into the United States as an alternative to the tax benefit in the form of a tax credit. An oil import fee should have two effects. It should reduce imports and promote conservation as a result of the increased price for foreign oil and gas. An oil import fee imposed as a matter of energy policy does not take into consideration the effect of that fee on the federal treasury or on the ultimate consumers of the oil and gas.

The current interest in an oil import fee in Congress is directed primarily toward reduction of the budget deficit.[65] Therefore, it is being considered almost solely as a revenue producing device. A recent Congressional Budget Office report indicates that an oil import fee of between two and ten dollars per barrel would reduce the federal deficit by about 10 billion dollars in fiscal year 1983, 9.4 billion dollars in fiscal year 1984, 10.5 billion dollars in fiscal year 1985, 13.2 billion dollars in fiscal year 1986, and 12.4 billion dollars in fiscal year 1987.[66] A recent report by the Congressional Research Service released by the House Government Operations Energy Subcommittee indicates that a $5.00 per barrel import fee would cut the deficit by 9.4 billion dollars in fiscal year 1982 but would increase it by 5 billion dollars in fiscal year 1984.[67] When making projections with respect to the amount of revenue which will be generated by an oil import fee, the effect of the consequent conservation must also be taken into consideration. An oil import fee of $2.00 per barrel would cause a daily demand for oil to drop by one hundred thousand to two hundred thousand barrels per day, whereas a $10.00 per barrel fee would probably cause a five hun-

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tial installation of insulation and residential solar and wind energy equipment. A tax credit was provided for producing fuel from an unconventional source, I.R.C. § 44D (Supp. V 1981), and for use of alcohol as a fuel. I.R.C. § 44E (Supp. V 1981). For businesses the investment credit percentage is increased from ten percent to as much as fifteen percent depending on the type of energy system investment. I.R.C. § 46(a)(2) (Supp. V 1981).

[65] *See* NEWSWEEK, Mar. 22, 1982, at 64.

[66] [1982] 81 DAILY TAX REP. (BNA) G-7.

[67] *Id.* at G-8.

dred thousand to one million barrel per day drop.[68] The decrease in the number of barrels on a daily basis would result in less revenue being collected as a result of the conservation measures taken to reduce the cost of imported oil. Consequently, the oil import fee mechanism would be a temporary measure. A high oil import fee levied to increase revenues would increase the conservation measures taken, which in turn would result in a reduction of revenues being collected.

When viewed from the energy policy standpoint rather than from a revenue producing standpoint, an oil import fee is desirable to curtail or limit dependence on imported oil if there are alternative domestic sources of energy available. In the absence of increased domestic exploration and production, or available alternative energy sources, the imposition of an import oil fee would have the effect of a self-embargo. Thus, increased conservation would be one desirable consequence of an oil import fee. Another desirable ramification from the energy standpoint is that the oil import fee would reflect the true cost of the natural resource. Theoretically, the oil import fee would account for the outflow of revenue from the federal treasury as a result of the foreign oil and gas extraction income tax which is credited pursuant to I.R.C. § 901, and it would include the cost of maintaining friendly relations with the oil producing sovereigns as a result of the United States foreign policy considerations.

From a national security standpoint, self-sufficiency is desirable. An energy policy which encourages self-sufficiency and reduces reliance on foreign oil imports also furthers national security objectives. Any future disruptions in the importation of foreign oil places a serious limitation on the freedom of the United States to conduct its foreign policy and severely restricts United States military deployment around the world. The United States must have secure suppliers of strategic materials such as oil and gas. There are relatively few secure sources of oil and gas at the present time. The Middle East is still in turmoil as a result of both the Arab-Israeli crisis and the Arab-Iranian crisis that is developing as Arab nations are banding together to block Iranian military and political objectives in the Middle East.[69] Thus, if the effect of the oil import fee is conservation and stimulation of domestic production and development of alternative energy sources, then the oil import fee is

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68 *Id.* at G-9.

69 NEWSWEEK, June 7, 1982, at 46.

also desirable from a national security policy viewpoint.

The most important political policy consideration with respect to the oil import fee is social equity. A major problem is deciding who should bear the burden of an oil import fee. The Consumer Energy Council of America claims that a fee on imported oil would increase heating bills in the United States by twenty-one billion dollars, cause a loss of up to three hundred thousand jobs, and wipe out the tax cuts of the Economic Recovery Tax Act of 1981.[70] Their major criticism seems to be that an oil import fee is a regressive tax and, therefore, falls most heavily on the poor who must spend a greater part of their income on energy for heating and transportation. Moreover, the impact of an oil import fee would not have an even geographic distribution but would fall most heavily on the northern United States, particularly the Northeast.[71] In addition to being geographically disproportionate, the cost would be disproportionately distributed by industry. Paper, steel, petrochemical, and chemical industries would not only pay the increased cost as a result of the imposition of the oil import fee but would also suffer supply problems as a result of the anticipated cutback in imports stemming from the higher price per barrel.[72] The Petroleum Industry Research Foundation estimates that a $5.00 per barrel import fee would increase inflation by about 1.3% in the first full year that it would be in effect, and the gross national product would fall off by nearly thirty billion dollars.[73] In a speech before the National Press Club the Chairman of the House Energy and Commerce Committee, who opposes the oil import fee, maintained that United States products would not be able to compete in international markets due to the increase in their prices as a result of the oil import fee.[74] In addition, an oil import fee which would result in conservation and decreased imported oil in the United States would have the effect of reducing the oil revenues of the oil producing sovereigns who would then have to absorb the cost of United States independence from their oil. The decreased demand for oil may add to the current glut of crude oil on the world market; however, that will result in an offsetting decrease in worldwide production of crude oil and a corresponding increase in

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[70] *See supra* note 66.
[71] *Id.*
[72] *Id.* at G-7 to G-8.
[73] *Id.* at G-8.
[74] *Id.; see supra* note 66 and accompanying text.

the per barrel price to offset the losses due to the decreased demand for crude oil in the United States. Those increased costs resulting from conservation in the United States will then be passed on to the ultimate consumer who must buy gasoline, heating oil, and petrochemical products.

IV. CONCLUSION

The development of a coordinated energy policy requires a fine tuning and adjustment of the competing policies served by a coordinated energy policy. National security, revenue raising, and social equity are all competing policies. A coordinated energy policy can only be developed by juxtaposing the underlying competing policies and making those adjustments that are necessary to suit the situation that arises. It follows, therefore, that a coordinated energy policy cannot be static but must be responsive to changing national policy needs.

The optimum national energy policy would be one which accomplishes the following objectives. The policy should encourage and support domestic exploration and extraction of oil and gas. Resources must be devoted to the development of alternative forms of energy such as solar, nuclear, wind, hydroelectric, other fossil fuels, and synthetic fuels. Importation of foreign oil must be encouraged, particularly from secure sources to make up the shortfall in United States production and to build up strategic reserves in order to protect against disruption of supplies and decrease the country's vulnerability. As the United States becomes more self-sufficient in energy, cutbacks should be made in imports of foreign oil beginning with the least secure suppliers. Simultaneously, the national energy policy must not wreak havoc with the national economy. Nevertheless, some tradeoff in inflation and higher prices for petroleum products may have to be made. While social equity is desirable, it is the user who derives the benefit; therefore, it is the user who should bear the true cost of the depletion of our natural resources.

The foreign tax credit tends to support maintaining our current level of petroleum imports if not actually promoting increased consumption of foreign oil and gas in the United States. The foreign tax credit should be retained to provide equality of tax impact for both domestic and foreign oil producers.

An oil import fee, on the other hand, discourages consumption of foreign oil in the United States and promotes conservation in addition to being a revenue raising device. As a matter of national security, an oil import fee is desirable if it decreases our dependence on foreign oil. With respect to social equity, an oil import fee is regressive and falls unevenly on the population both geographically and by industry. As a revenue measure, its long term effect is not desirable, but as an energy measure it would promote conservation and reflect the true cost of a diminishing natural resource. No import fee should be imposed until such time as the United States attains a higher degree of self-sufficiency.

Repeal of the Windfall Profits tax coupled with deregulation should provide the incentive to find more domestic oil and gas at whatever cost the market will support.

Social equity can be accomplished through the tax law by allowing tax credits or rebates to lower income persons or specific industries to lighten their burden.

It is time for a coordinated national energy policy in which the revenue laws support the goals of that national energy policy.

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