



BUREAU OF COMPETITION

UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

V890072

COMMISSION AUTHORIZED

May 12, 1989

The Honorable Jennings G. McAbee
Chairman
Other Taxes and Revenues Subcommittee
Ways and Means Committee
South Carolina House of Representatives
P.O. Box 11867
Columbia, South Carolina 29211

Dear Chairman McAbee:

The staff of the Federal Trade Commission¹ is pleased to submit this letter in response to your request for comments on the potential competitive effects of House Resolution 3899, which would require that wholesale gasoline prices be rolled back to their levels as of April 1, 1989. Your letter notes that H.R. 3899 has been referred to your Subcommittee and will be the subject of a public hearing on May 15, 1989. We believe that, if enacted, H.R. 3899 may have unintended adverse consequences for South Carolina consumers.

Interest and experience of the Federal Trade Commission

The Federal Trade Commission is charged by statute with preventing unfair methods of competition and unfair or deceptive practices in or affecting commerce. 15 U.S.C. § 45. Under this statutory mandate, the Commission seeks to identify restrictions that impede competition or increase costs without offering countervailing benefits to consumers. In particular, the Commission and its staff have had considerable experience assessing the competitive impact of regulations and business practices in the oil industry.²

¹ These Comments are the views of the staff of the Bureau of Competition of the Federal Trade Commission. They are not necessarily the views of the Commission or any individual Commissioner. Questions about these comments may be addressed to Ronald B. Rowe, Assistant Director, Bureau of Competition, room 3301, 601 Pennsylvania Avenue, N.W., Washington, D.C. 20580. Mr. Rowe's telephone number is (202) 326-2610.

² The Commission's staff has gained extensive experience with energy competition issues by conducting studies, investigations, and law enforcement actions. FTC staff comments
(continued...)

Description of H.R. 3899

Section 1 of H.R. 3899 would roll back the "wholesale prices of gasoline in this State . . . to the base price of this gasoline as of April 1, 1989, as it entered this State from the refineries or suppliers located outside this State." Section 2 would permit prices above the rollback prices "in order to comply with contractual provisions that require the same pricing for multistate outlets or in order to comply with any other contractual provisions in existence on April 1, 1989." However, such "excess wholesale prices . . . are declared to be a surtax . . . for purposes of funding the South Carolina SHIMS highway program." Section 3 provides that Sections 1 and 2 will expire "six months after the effective date of this act"

The price control regulatory features of H.R. 3899 may lead to shortages and higher gasoline prices

Enactment of H.R. 3899 may have unintended adverse consequences for South Carolina consumers. The proposed law would mandate the lowering of wholesale gasoline prices. However, nearly all of the gasoline sold by wholesalers in South Carolina originates with refiners located elsewhere who distribute such product in a large number of States. If mandated wholesale price levels have an adverse impact on the profitability of overall gasoline distribution for out of state refiners or other wholesale distributors, South Carolina may suffer a net loss of wholesale gasoline availability as products are diverted to markets with no governmental constraints upon individual commercial pricing decisions. It is possible, moreover, that dislocations caused by enactment of H.R. 3899 may arise and continue beyond the six-month duration of the proposed legislation.

The concern over shortages is not merely a hypothetical possibility. The price ceilings imposed in the federal price and allocation regulations under the Emergency Petroleum Allocation Act ("EPAA")³ resulted in shortages. The regulatory response to

²(...continued)

and testimony to legislative bodies have identified the costs of proposed gasoline retailing divorcement and "below-cost selling" legislation for North Carolina, South Carolina, Georgia, Alabama, Tennessee, Washington, Hawaii, Nevada, and for the United States Senate and House of Representatives. The Commission and its staff have also gained considerable experience with gasoline refining and marketing issues affecting consumers from premerger antitrust reviews pursuant to Sections 7 and 7A of the Clayton Act, 15 U.S.C. §§ 18, 18a.

³ Pub. L. No. 93-159, 87 Stat. 619.

these shortages was an enormously complex price and allocation system that attempted to alleviate this problem but was unsuccessful.⁴

The dangers associated with holding wholesale energy prices below market clearing levels are also aptly illustrated by the Federal government's experience with regulating wholesale natural gas prices. Beginning in 1954, the Federal government began to set the "wellhead" price of natural gas sold to interstate natural gas pipelines. During the 1970s, shortages of gas began to appear in the interstate gas markets. One of the reasons for this shortfall in interstate gas deliveries was that gas was flowing to intrastate gas pipelines, which were not constrained in the price they could pay for gas. Intrastate pipelines in the gas producing states could outbid their interstate rivals for gas because intrastate prices were not regulated. To alleviate these shortages, Congress passed (in 1978) the Natural Gas Policy Act and the Power Plant and Industrial Fuels Use Act, which were intended to remove the price differences between intra- and interstate gas. As these price differences disappeared, so did the accompanying shortages. The wholesale gasoline prices mandated by H.R. 3899 could result in a similar diversion of gasoline away from South Carolina consumers.

The Commission's Bureau of Economics and Competition have surveyed the adverse effects of price controls in energy industries.⁵ These analyses suggest that you may wish to conduct a legislative inquiry on both the need for such legislation and its likely effects on competition.⁶

⁴ See C. Roush, Effects of Federal Price and Allocation Regulations on the Petroleum Industry, 10-14 (FTC Staff Report 1976); S. Harvey & C. Roush, Petroleum Product Price Regulations: Output, Efficiency and Competitive Effects, 169-180 (FTC Staff Report 1981).

⁵ I am enclosing copies of the following reports or comments prepared by the Commission's staff for your subcommittee's consideration: Roush, supra note 4; Harvey & Roush, supra note 4; Bureau of Economics, Comments Concerning Effects of Federal Price and Allocation Regulations on the Petroleum Industry (1976); Bureau of Competition, Comment on the Scope of the No. 2 Distillate Proceedings, (1979) (FTC staff comment to Economic Regulatory Administration).

⁶ To the extent H.R. 3899 is premised on the belief that gasoline prices are artificially high because of anticompetitive behavior by wholesalers of gasoline, the federal antitrust laws are sufficient to address such behavior. While we are unaware of
(continued...)

Conclusion

For the reasons stated above, we believe that H.R. 3899, if enacted, could injure commerce, competition, and consumers in South Carolina. If gasoline shortages were to result from its passage, a return to gasoline lines could occur, and gasoline prices could rise to an inflated level in South Carolina. Because there may be costs associated with restoring supplies diverted from South Carolina by H.R. 3899, any rise in gasoline prices might endure beyond the six month expiration date of the proposed legislation.

We appreciate the opportunity to comment on H.R. 3899. Please feel free to call on us if we can be of further assistance.

Sincerely,


Jeffrey I. Zuckerman
Director

⁶(...continued)
any evidence supporting that position, we would be interested in hearing from anyone with such evidence.