DRILLING FOR A SOLUTION: FINDING WAYS TO CURTAIL THE CRUSHING EFFECT OF HIGH GAS PRICES ON SMALL BUSINESS

HEARING

BEFORE THE

SUBCOMMITTEE ON AGRICULTURE,
ENERGY AND TRADE

OF THE

COMMITTEE ON SMALL BUSINESS
UNITED STATES
HOUSE OF REPRESENTATIVES

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HEARING ON DRILLING FOR A SOLUTION: FINDING WAYS TO CURTAIL THE CRUSHING EFFECT OF HIGH GAS PRICES ON SMALL BUSINESS

THURSDAY, APRIL 14, 2011

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS, SUBCOMMITTEE ON
AGRICULTURE, ENERGY AND TRADE,
Washington, DC.

The Subcommittee met, pursuant to call, at 10:00 a.m., in Room 2360, Rayburn House Office Building. Hon. Scott Tipton [chairman of the Subcommittee].

Present: Representatives Tipton, Fleischmann, Landry, Critz.

Chairman TIPTON. Well, good morning everyone. I would like to thank you for joining us for this hearing and it will now come to order.

This is our first Subcommittee hearing and the subject truly could not be more timely or important. Rising oil and gasoline prices have a crippling effect on small businesses, as well as our overall economy. In fact, just this morning the headline of the Washington Examiner—I will even grab this—it says gas prices hobble small businesses. When we look at yesterday's Washington Post, $4 a gallon gas fuel fears stymie our recovery here.

I would like to extend special thanks to each of our witnesses for making this trip to Washington, D.C., and taking time out of your busy schedules. I would especially like to welcome Jim Ehrlich today, who is a constituent of mine out of Colorado.

Today we will hear directly from small businesses on how increased fuel prices have affected their bottom lines and ability to expand and be able to create jobs. Small businesses have been hit especially hard by high fuel prices. In addition to driving up the costs of transportation for their goods and services, the spike in gas prices is drying up consumers for many of our small businesses. Just yesterday, Walmart's chief executive officer told the Washington Post that the retail giant's number of customers is increasing with rising gas prices. In an effort to tighten up their budgets by driving less, consumers tend to consolidate their shopping trips to one larger box store to be able to do their shopping rather than going to a handful of community shops where they would normally visit.

This trend is even more alarming when taking into consideration that many communities across our country have already seen their consumer bases dwindle in conjunction with staggering unemploy-

ment. We are essentially watching the extinction of the mom-and-pop shops play out before our very eyes.

Retailers, of course, are not the only ones feeling the pinch of high gas prices. As we will hear today, it is hitting our farmers, our ranchers, especially hard, and any business that relies on fuel to send or receive their goods and services. This increased cost of doing business is either absorbed by the company, diverting resources away from investment and expansion, or passed along to cash-strapped consumers who have already tightened their belts in cutting back. In either case, it is a roadblock to economic security in this country, economic recovery, and job creation.

In this country, in addition to hearing testimony today, we will be talking about the direct impact high fuel prices are having on small businesses. We will explore the root causes of these rising costs, including overregulation and punitive taxation on the energy industry. We will look at possible solutions to jumpstart the energy exploration and production in our country and discuss the need for the U.S. to embrace an "all of the above" energy platform that includes wind, solar, oil, natural gas, and coal. I look forward to hearing from our witnesses as they provide testimony today, and we seek to find solutions to curb the effects of high gas prices on small businesses.

I would now like to recognize our ranking member, Member Critz, for his opening statement.

Mr. CRITZ. Thank you, Mr. Chairman. And before I go into my statement I just wanted to thank the witnesses for coming today to talk about the gas prices, but also to thank Scott, our chairman. He and I have had a couple of meetings, a couple of talks, and it looks like we are going to have a very productive Subcommittee. I am looking forward to working with him on this issue and on many issues that face small businesses.

Small businesses play a key role in the economy creating nearly two-thirds of net new jobs. However, with gas prices rising, their contributions to this growth may be jeopardized. In the last 3 months, oil prices have reached a 30-month high exceeding $112 per barrel. With the U.S. importing more than 200 million barrels of oil per month, the cost of doing so is substantial. Many analysts are suggesting that these increases could lead to gas prices of $5 or more per gallon. Small businesses are drivers of economic progress, but a recent report shows that surges in energy prices are a top concern among them. According to the PNC Economic Outlook Survey of Small Firms, nearly three-quarters responded a sustained rise in energy prices would have a negative impact on their business potentially restraining growth.

In order to deal with these price increases, small businesses are often faced with two choices. They can either absorb the costs or pass them on to their customers. Absorbing the higher prices creates financial challenges resulting in less capital to expand their business or hire new employees. Passing the cost increases on to consumers can reduce demand for a firm's goods and services. Neither are preferable alternatives and this is why we must find a solution.

Whether these solutions focus on increasing supply or reducing demand, it is clear that the status quo is not an option. Steps must

be taken to increase U.S. energy independence. While much of the price increases are tied to the uprisings occurring in Northern Africa and the Middle East, growing demand as the global economy recovers is also a significant part of this equation. Increasing the supply of oil can lead to lower gas prices. While there are several options to do so, one of the most promising is increasing access to potential oil resources under the U.S. Outer Continental Shelf, particularly in deepwater areas.

The Department of Energy projects that oil production would increase from 5 million barrels per day to 7.3 million barrels per day by 2030 with a complete access to this area. Doing so could lead to greater domestic oil reserves and ultimately reduce prices for all consumers of gas, including small businesses.

Another important energy alternative is to increase the use of oil shale. I know the Green River Oil Shale Formation in Colorado, Utah, and Wyoming is estimated to hold the equivalent of 1.38 trillion barrels of oil equivalent in place. The Marcellus Shale is the largest unconventional natural gas formation in the United States. Until recently, the natural gas in the Marcellus Shale was locked in an impermeable layer of rock which made the natural gas uneconomical to extract. However, with the advent of new drilling technologies coupled with the rising demand for domestic natural gas, the development of the Marcellus Shale has increased exponentially in states such as Pennsylvania, Ohio, and West Virginia.

The shale is estimated to hold 4.9—excuse me, 493 trillion cubic feet of extractable natural gas currently valued at more than $1.8 trillion. As with most economic activity, the impacts of the natural gas affect more than just the specific firms directly involved in the industry. There are also important employment and income effects on local businesses who supply the industry, such as oil-filled service companies, restaurants, retailers, and hotels, in addition to effects that result from employees spending their wages locally.

In Pennsylvania, 75 percent of the natural gas it uses every day is being imported. The Marcellus Shale Formation holds enough recoverable natural gas reserves to not only serve Pennsylvania's needs but to turn our country into a significant exporter of energy generating equally significant economic benefits. This is incredible when you think back to 10 years ago when we were only discussing the importation of this gas. The high-paying jobs available today in the Marcellus Shale gas industry are expected to multiply in the future, meeting the needs of gas companies' efforts to increase drilling and production across the region. In Pennsylvania alone it is estimated that more than 110,000 new jobs have been created because of the development of this shale.

I would just like to emphasize that as long as we develop this shale in an environmentally responsible manner, its potential is monumental. This is an immediate source of alternative energy that is currently being tapped. Excuse me. As our country continues to develop new sources of energy, carbon capture and sequestration technology allows it to continue using coal as a base load fuel while capturing and sequestering the carbon emissions that would have otherwise been released into the atmosphere.

The United States has enough coal to meet projected energy needs for almost 200 years. Here again is another immediate

source of alternative energy. While supply-related options show great promise, there are equally important policy options that could reduce demand. Reducing the use of gas by improving energy efficiency measures could also lead to lower prices. Small businesses can readily do this by adopting new technologies such as replacing gas-based vehicles with hybrid flex-fuel or electric-based cars and trucks. This would lessen their and our nation's need for oil. By doing so, entrepreneurs would face less volatility in their energy costs.

Several initiatives are spearheading the replacement of gas-based vehicles. Small businesses have been encouraged to purchase more fuel efficient vehicles through tax credits, including gasoline electric hybrids and plug-in electric vehicles. In addition, substantial funding has been provided to advance research into alternative automotive energy and fuel cell technologies. As commercialization occurs, small businesses will have a broader array of energy efficient vehicles to choose from. Whether it is increasing the domestic supply of oil or decreasing demand, everything should be on the table to help reduce U.S. dependence on foreign oil. Doing so will not only benefit small businesses and consumers but will increase our nation's energy security as we can reinvest savings into alternative fuels.

In this regard, I am particularly looking forward to hearing the witnesses' views on policy options and what effect they could have on prices. If we do nothing, rising gas prices have the potential to dramatically impact small businesses and disrupt the recovery we are currently experiencing. If small firms are going to lead the economy forward and create new jobs, they need greater predictability and less volatility in the prices they pay for energy. I hope today's hearing is a step forward in this direction.

Thank you, Mr. Chairman. I yield back.

Chairman TIPTON. Well, thank you, Ranking Member Critz. Talking about developing energy here at home we are going to get along just fine. I do appreciate that.

I am a small businessman. This is the first Committee hearing that I am chairing. I would like to thank our chairman for having the privilege of being able to do this. Sam is very gracious. And I would also like to give a tip of our hat to our staff as well. A lot of the work that goes on behind the scenes to be able to put one of these together is extraordinary. And I really appreciate all of the help. And Mindi, thank you for your help as well.

So if other Committee members do have an opening statement prepared I would ask that they submit that for the record today.

And I would like to take a moment, gentlemen, to be able to explain our lighting system in front of you. You will each have five minutes for your testimony. The light will start out as green. Once it gets to the four-minute level it will then turn to yellow, and at the expiration of time it will then turn red. And I would ask that you wrap up your comments at that point and we would appreciate it as you finish.

STATEMENTS OF JIM EHRLICH, EXECUTIVE DIRECTOR, COLORADO POTATO ADMINISTRATIVE COMMITTEE; RICK RICHTER, OPERATOR, RICHTER AVIATION; PRESIDENT, NATIONAL AGRICULTURAL AVIATION ASSOCIATION; DICK PINGEL, OWNER, FINALLY TRUCKING, INC.; ROBERT WEINER, PROFESSOR, INTERNATIONAL BUSINESS, PUBLIC POLICY AND PUBLIC ADMINISTRATION AND INTERNATIONAL AFFAIRS, GEORGE WASHINGTON UNIVERSITY

Chairman TIPTON. So it is my pleasure right now to be able to introduce our first witness today, a constituent of mine, Mr. Jim Ehrlich.

Jim is the executive director of the Colorado Potato Administrative Committee, representing a significant industry in my home district. Jim, we appreciate you being here today and we look forward to your testimony.

STATEMENT OF JIM EHRLICH

Mr. EHRLICH. Well, I would like to thank Chairman Tipton and the Committee for inviting me today.

I speak on behalf of the 170 different potato growers in the San Luis Valley of South Central Colorado. These growers typically produce about 2.2 billion pounds of potatoes a year with a market price of 175– to $240 million depending on the price of potatoes that year. The San Luis Valley is a high alpine desert, base elevation of 7,600 feet with less than 7 inches of moisture annually. Irrigation supplies are dependent on abundant snowpack and sustained utilization of a vast underground aquifer. Colorado ranks as the second largest shipper of fresh market potatoes in the country, a fact that many people do not know.

This 6-county region of Colorado is dependent upon agriculture as the economic engine for the valley's 50,000 residents. Unfortunately, we possess some of the poorest counties in Colorado with many rural families having incomes below poverty level and without opportunity for better jobs.

Today I am going to focus on three things: the impact of high energy prices and gas prices on potato producers in the valley, the inability of the United States to increase domestic production of our vast energy reserves, and the cost of regulation to potato producers, the impact of high energy and gas prices on potato producers.

I recently read a report claiming that for every 10 cent increase in gas prices there is a net loss of $5 billion to the United States' economy. When you consider the fragile state of the worldwide economy and our economy in the United States, this has great significance. When you consider that petroleum-based products are the only source for most of the transportation needs in the world today, there is no real mystery why when you have one supply and limited supply of that one item and worldwide demand is growing like it is, why there is a problem.

Agriculture requires energy as a critical input to production. Potato production uses energy directly as fuel and electricity to operate tractors and equipment, cool potato cellars, process and package product indirectly, and fertilizers and chemicals produced off the farm but needed as critical inputs for crop production. Total en-

ergy costs of an irrigated potato crop in the San Luis Valley can be as great as 50 percent of the total production expenses.

Unlike areas of the country where irrigation is unnecessary or no-till practices are common, this is not the case with potato production in the San Luis Valley. It requires large amounts of electricity to irrigate and large amounts of tillage. Crop must be stored at the correct temperature and humidity year round to ensure marketable condition for consumers. The crop must be shipped in refrigerated trucks to distant markets across the country throughout the year.

So what happens when gas prices rise like they have this year? Because farmers are price takers and lack the capacity to pass on higher costs through the food marketing chain, the net result is a loss in farm income. The reality is prices of most fuel sources tend to move together. So as gas prices typically rise, other energy prices rise in concert. Fertilizer prices are dependent upon natural gas prices and potatoes require large amounts of nitrogen, phosphate, and pot ash fertilizers. Harvest, sorting, grading, and shipping are all heavily mechanized energy-dependent steps. The San Luis Valley is located in an isolated mountainous region. High diesel prices affect freight rates and truck availability cutting into the growers' bottom line.

The economic reality for our area is when gas prices rise, farmers make less money. The local economy suffers because it is dependent on the farmers. Farmers are forced to cut back on expenditures and this lack of economic activity impacts local businesses and communities, school districts, et cetera, the inability of the United States to increase domestic production of vast energy reserves.

Because the United States relies on imported sources of oil for over 60 percent of our oil needs, we export wealth daily, primarily to countries that are hostile to us. This not only causes economic stress but is a threat to our national security. Without a stable source of relative economical energy for agriculture, our nation's food security is at risk also, and as a result, our national security. As the proud father of a U.S. Marine serving in Afghanistan currently, I speak from my heart.

I recently read a report from the Congressional Research Service detailing the potential fossil fuel reserves of the world. This report came out in December. I was encouraged to see the United States might actually have the largest fossil fuel reserves in the world, but I was distraught because as a country we continually fail to develop these resources. It is time to find bipartisan solutions to develop all energy resources available in this country, including alternative energy sources. Energy prices are going to continue to rise with increasing worldwide demand, even if we develop every source of energy we have available as quickly as possible. Failure to act puts our great nation and its ability to feed the world at risk.

The last thing I want to talk about is the cost of regulation to potato producers. I encourage the Committee to consider the economic impact overregulation has on agriculture and small businesses across the country. Any new regulation should be thoroughly analyzed for the often unintended economic consequences that result. I applaud the recent House vote to prevent unneces-

sary NPDES permits that were actually being forced on agriculture without just cause.

As a nation, we have to respect and consider everyone's opinion when we make decisions affecting the environment, food safety, school meal plans, et cetera. But as elected officials, you have the responsibility to create laws that carefully represent the beneficial interest of the majority of citizens. It is not impossible to please all interests and I know this because I work with farmers and make progress.

An example of this overregulation is the EPA. I cannot even begin to go there but I will point out one example. They are proposing dust regulations for rural America and they do not have the data to show that these regulations are an actual problem. They do not even have a rural dust monitoring network. The reality is rural America is dusty. Potatoes grow in the dirt, the good dirt that feeds all of us.

In closing, I would like to thank the Committee for the opportunity to testify today. Colorado potato growers are very grateful for the work you are doing and the commitment you have to agriculture and our nation. Thank you very much.

[The statement of Jim Ehrlich follows:]

Colorado Potato Administrative Committee
1305 Park Ave.
Monte Vista, Colorado 81144

April 11, 2011

Chairman - Honorable Representative Scott Tipton
House of Representatives- Subcomittee on Agriculture, Energy, and Trade

Dear Chairman Tipton and committee members,

I want to thank Chairman Tipton and the committee members for the opportunity to speak today on behalf of the Colorado Potato growers in the San Luis valley of southern Colorado. As executive director of the Colorado Potato Administrative Committee, the state and federal marketing order for potatoes in the San Luis valley I represent over 170 potato farmers. These growers typically produce over 2.2 billion lbs. of potatoes annually with a typical economic return to the growers between $175-240 million, depending on the market price of potatoes. The San Luis valley is a high altitude alpine desert, base elevation 7600 ft., with less than 7 inches of moisture annually. Irrigation supplies are dependent on abundant snowpack and sustainable utilization of a vast underground aquifer. Our growers produce some of the highest quality potatoes in the United States. Colorado ranks as the second largest shipper of fresh market potatoes in the country with over 90 percent of our crop being marketed as fresh table stock.

This six county region of Colorado is dependent on agriculture as the economic engine for the valley's nearly 50,000 residents. The area is predominately rural with the largest city of Alamosa having a population of less than 10,000 when the students are in session at Adams State College. Unfortunately, we possess some of the poorest counties in Colorado with many rural families having incomes below poverty level and without the opportunity for better jobs.

I want to focus my testimony on three areas;

- The impact of high energy and gas prices on agricultural producers,
- The inability of the United States to increase domestic production of our vast energy reserves, and
- The cost of regulation to agricultural producers

The impact of high energy and gas prices on agricultural producers

I recently read a report claiming that for every $.10 increase in gas prices there is a net loss of $5 billion dollars to the United States economy. When you consider the fragile state of the worldwide economy today this number has even greater significance. When you consider that petroleum based products are the only source for most of the transportation needs of the entire world there is real no mystery why limited supplies result in rising prices when worldwide demand is growing rapidly.

Agriculture requires energy as a critical input to production. Potato production uses energy directly as fuel or electricity to operate tractors and equipment, cool potato cellars,

process and package product, and indirectly in fertilizers and chemicals produced off the farm but needed as critical inputs for crop production. Total energy cost of an irrigated potato crop in the San Luis valley can be as great as fifty percent of total production expenses. Unlike areas of the country where irrigation is unnecessary or no-till practices are the norm, potato production requires intense irrigation dependent on electricity. Growers must use intensive tillage for a crop that is dependent on loose, friable soil conditions for proper tuber development and quality production. The crop must be stored at the correct temperature and humidity to insure marketable condition for a year round supply to satisfy consumer demand. The crop must be shipped in refrigerated trucks to distant markets across the country throughout the year.

So what happens when gas prices rise like they have this year? Because individual farmers are "price takers" and lack the capacity to pass on higher costs through the food marketing chain the result is net farm income will be reduced. The reality is prices of most fuel sources tend to move together so as gas prices rise typically other energy prices rise in concert. Fertilizer prices are dependent on natural gas prices and potatoes require large amounts of nitrogen, phosphate, and potash fertilizers. Harvest, sorting, grading, and shipping are all heavily mechanized energy dependent steps. The San Luis valley is located in an isolated mountainous region where winter can be fierce. High diesel prices affect freight rates and truck availability cutting into a grower's bottom line. The economic reality for our area is when farmers make less money the local economy suffers. Farmers are forced to cut back on expenditures and this lack of economic activity impacts local businesses and communities.

The inability of the United States to increase domestic production of our vast energy reserves

Because the United States relies on imported sources of oil for over 60 percent of our oil needs we export wealth daily, primarily to countries that are hostile to us. This not only causes economic stress but is a threat to our national security. Without a stable source of relatively economical energy for agriculture our nation's food security is at risk and as a result our national security. As the proud father of a U.S. Marine currently serving in Afghanistan I am speaking from my heart when I write these thoughts.

I recently read a report from the Congressional Research Service detailing the potential fossil fuel reserves of the world. I was encouraged to see that the United States might actually have the largest fossil fuel reserves in the world but I was distraught because as a country we continually fail to develop these resources. It is time to find bi-partisan solutions to this embarrassing failure to develop all energy sources that are available. Energy prices are going to continue to rise with increasing worldwide demand even if we develop multiple sources of energy as quickly as possible. Failure to act puts our great nation and its ability to feed the world at risk.

In the San Luis valley potato growers are working within a local coalition to explore community based solar energy development. We are doing this to develop the abundant natural resource we are blessed with, and encourage economic development within the region. We recognize the need for sustainable energy development and fear the lack of energy availability in the future unless our nation's energy policies change. The reality is solar energy doesn't currently make economic sense but it will as energy prices continue

to spiral higher. This process has met and will continue to experience opposition over transmission line location, which provides a convenient transition to my last comment.

The cost of regulation to agricultural producers

I encourage the committee to consider the economic impact over-regulation has on agriculture and small business across the country. Any new regulation should be thoroughly analyzed for the often unintended economic consequences that may result. I applaud the recent House vote to prevent the unnecessary NPDES permits that were being forced on agriculture without just cause. As a nation we must respect and consider everyone's opinion when we make decisions affecting the environment, food safety, school meal plans, etc. But as elected officials you have the responsibility to create laws that carefully represent the beneficial interest of the majority of citizens. It is not possible to please all interests and make progress. As an example potato growers should have to observe Good Agricultural Practices, but they should not have to follow the same practices as onion growers or lettuce growers. The potato industry is currently burdened with unnecessary food safety audits because retailers mandate them out of fear or as a marketing tool, not because potatoes have realistic science based risk levels. Another example is the Environmental Protection Agency proposing dust regulations for rural American when they don't have data from rural areas to show there is an actual problem. The reality is rural America is dusty and potatoes grow in the dirt. The good dirt that feeds us all.

In closing I would like to finish with a comment about the need for a transmission line for solar development in the San Luis valley. Currently there is only one transmission line serving the entire valley. The utility companies have identified the need for redundant service because of capacity issues and for solar energy development that would provide badly needed economic growth. Opponents to the transmission line basically are opposed because they want it located somewhere else, away from their property or view. I imagine there was the same type of local opposition when the railroads were built or the existing transmission line first provided electricity to the valley. The difference today is the regulatory process is used blatantly to prevent thoughtful progress for the majority of citizens.

Thank you for the opportunity to testify today. Colorado potato growers appreciate your commitment to agriculture and our nation, and we are grateful for your efforts.

Respectfully,

Jim Ehrlich
Executive Director
Colorado Potato Administrative Committee

Chairman TIPTON. Thank you very much, Jim. I appreciate your testimony.

Our next witness is Mr. Rick Richter, who has flown as an agricultural pilot for over 32 years and is the proprietor of Richter Aviation. He is the current president of National Agricultural Aviation Association and represents them in his testimony today. Mr. Richter.

STATEMENT OF RICK RICHTER

Mr. RICHTER. Thank you, Chairman Tipton, Ranking Member Critz, and all members of the Subcommittee for the opportunity to testify on the effects that the increase in fuel prices have on small aerial application businesses.

My name is Rick Richter, owner of Richter Aviation, an aerial application business in Maxwell, California. And I am testifying today on behalf of the National Agricultural Aviation Association, also known as the NAAA, of which I am the 2011 president.

NAAA is a national association which represents the interests of small business owners and pilot licensed as commercial applicators that use aircraft to enhance the production of food, fiber, and biofuel, protect forestry and control health threatening pests.

Aerial application accounts for an estimated 18 percent of commercially applied crop protection products in the United States and is often the only method for timely pesticide application, especially when wet soil conditions, rolling terrain, or dense plant foliage presents the use of other methods of treating an area for pests.

The average aerial application business consists of two operating aircraft, four people, including two pilots, a mixer-loader, and an administrative staffer. Increases in fuel prices result in a number of cash flow and service marketability issues for the aerial application industry. And, of course, the price of fuel for agriculture will trickle down to the end consumer of food.

According to the United Nations' Food and Agricultural Organization, food prices reached a record high in February, and prices in March of this year remain 37 percent higher than those in March of 2010.

At the beginning of the season, an aerial applicator sets a base price per acre treated by air based on the expected cost of operation. This is the amount he charges his farmer clients. Depending on the type of fuel used, of which there are two—avgas for piston engineered aircraft and Jet A for turbine engine ag aircraft—an operator includes a base price for fuel going into the season. Some applicators stick with this price regardless of fluctuations in fuel price, and as a result may lose money when prices go up steeply. Other applicators will incorporate a fuel surcharge into their pricing structure.

Incorporated within that fee per acre charge is the fuel charge which is based on an average price of fuel per gallon. This ranges but on average it is estimated to be about $2 per gallon. If fuel rises above that figure, a fuel surcharge is added, and a typical fuel surcharge is the difference between the average price for a gallon of fuel that an applicator builds into his acre charge and the price of a gallon of aviation fuel at the time of application, assuming that the latter is a greater amount, multiplied by the average number

of gallons burned by that particular aircraft in an hour multiplied by the amount of time it took to make the application for the farmer.

Fuel surcharges in our industry have been met with minimal complaint by farmer clients as of late because they will be getting a good price for the crop. If this was 2002 and we were faced with the same high prices for fuel that we are facing today but ag commodity prices were two to three times lower than what they are today, our industry would be facing some real challenges. As of April 6, 2011, the wholesale price of Jet A without taxes was $3.33 per gallon as quoted by a large Southeast U.S. fuel supplier. If in 2002 when commodity prices were much lower and Jet A fuel for turbine-powered ag aircraft was the same price today or the same price that it was at its height in 2008 when it averaged $4.72 per gallon, it would be much tougher for a farmer to embrace a fuel surcharge for aerial application services rendered.

Realistically, when input prices such as fuel are high and commodity prices are low, a significant drop in the use of aerial application services and other farm services would occur as a result of containing costs. Well, this helps the farmer contain expenses but frequently results in less yield and poor crop quality, hence negatively affecting his revenue potential. The lack of application work is a challenge for an aerial application operator that requires steady business each season to remain viable.

Another challenge that aerial applicators face, particularly when fuel prices are high, is the financial terms that fuel suppliers have for payment of their fuel and how those terms differ from their own accounts receivable terms. The typical payment term that an aerial applicator has with his fuel supplier is 10 days with established credit. This usually differs from payment terms that aerial applicators' customers are accustomed to paying, which is typically between 45 and 60 days. This can pose challenges because fuel costs consist of approximately 20 percent of an aerial applicator's total expenses. If the average ag aircraft burns 50 gallons per hour and is flown 300 hours per season and there are 2.2 aircraft on average per aerial application operation, then 38,600—excuse me, 36,816 gallons of fuel will be required.

When an applicator is facing a deficit in accounts payable compared to his accounts receivable and outlaying large chunks of capital for fuel particularly when the price of fuel is high, this may result in sizeable interest payments for small aerial application businesses. It is widely expected that higher interest rates will return and coupled with the greater demand for fuel globally will likely lead to a steady increase in the price of fuel and place much greater cost pressures on small aerial application businesses. High fuel cost conditions in some instances do lead to aerial applicators taking more risk in trying to hedge the price of fuel by filling up their tanks early and storing fuel. But storing for too long of a period can result in developing moisture in the fuel, algae problems in Jet A, and possibly evaporation of avgas.

One other issue of concern to the agricultural aviation industry that is related to fuel supply is an effort underway to phase out the use of avgas. EPA has mentioned the possibility of a new environmental standard associated with avgas due to its emissions of lead

in the air and calls by environmental activists to ban the fuel completely. Avgas is used in 51.87 percent of ag aircraft in the U.S. today. NAAA's primary concerns are with the safety and feasibility issues associated with mandated a shift from avgas. NAAA has encouraged the EPA and the FAA to allow time for and devote resources toward the development of a suitable alternative to avgas before imposing avgas regulations or banning the use of the fuel altogether. NAAA urged the agency to consider the detrimental economic impacts that could occur to our industry and the farmers that rely on us should avgas be phased out prior to the development of a safe and practical alternate fuel. Piston engines are a notably less expensive engine for ag aircraft compared with turbine engines and for smaller aerial application businesses it may be the only affordable type of power plant available.

Chairman Tipton, Ranking Member Critz, thank you very much for the opportunity to explain these issues affecting the aerial application industry in regards to the increase in fuel prices and supply for ag aviation aircraft. More detail on the issue and how it affects the aerial application industry can be found in the written comments that we have submitted. A national policy that can be developed that would ensure a stable price and supply for Jet A and avgas is imperative for our industry and the farmer clients we treat. Also, continuation of the fuel tax exemption for aviation fuel used for large aircraft while flying over the farm has provided some relief to our farmer customers.

Our industry provides a valuable service in aiding in the production of the safe, affordable, and abundant global supply of food, fiber, and biofuel, and as such, a steady supply and price of fuel is vitally important to us and our farmer customers. Thank you again to you and the members of the Subcommittee.

[The statement of Rick Richter follows:]

April 14, 2011

Testimony of the
National Agricultural Aviation Association

Submitted to The United States House of Representatives

Small Business Committee,
Subcommittee on Agriculture, Energy & Trade

Regarding
Effects of Fuel Prices on Small Aerial Application Businesses

Thank you, Chairman Tipton, Ranking Member Critz and all members of the Subcommittee for the opportunity to testify on the effects the increase in fuel prices have on small aerial application businesses. My name is Rick Richter, owner of Richter Aviation in Maxwell, California and I am testifying today on behalf of the National Agricultural Aviation Association, also known as NAAA, of which I am the 2011 president. NAAA is a national association which consists of more than 1,600 members in 46 states, and represents the interests of small business owners and pilots licensed as commercial applicators that use aircraft to enhance the production of food, fiber and bio-fuel; protect forestry; protect waterways, pastureland and ranchland from invasive species; and control health-threatening pests.

Aerial application accounts for an estimated 18 percent of commercially applied crop protection products in the United States and is often the only, or most economic, method for timely pesticide application. It permits large and often remote areas to be treated rapidly, thus ensuring timely and efficient service. When wet soil conditions, rolling terrain or dense plant foliage prevents the use of other methods of treating an area for pests, aerial application may be the only remaining method of treatment.

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NAAA members are small businesses providing pest control services to approximately 100 or more customers annually, and often operating across several states in their work. The average aerial application business consists of two operating aircraft and four people (two pilots, a mixer-loader and an administrative staffer).

I have been an ag pilot for 32 years and an aerial application small business owner since 1983. My wife Brenda and I have a fleet of four Ag-Cat aircraft and seeded and treated more than 33,000 acres of rice last year. We also treated alfalfa, almonds and wheat. Our business employs 12-14 people during the busy flying season from April to August and I also farm 450 acres of rice on my own.

Increases in fuel prices in the aerial application industry results in a number of cash-flow and service-marketability issues for the aerial application industry. And of course, the price of fuel always tends to trickle down all the way to the last entity in the supply chain from the applicator to the farmer to the retailer and ultimately to the consumer. According to the United Nations Food and Agriculture Organization, food prices reached a record high in February, and prices in March of this year remained 37 percent higher than those in March 2010. Additionally, the FAO warns food prices may continue to rise and, "it would be premature to conclude that this is a reversal of the upward trend."

At the beginning of the season, the aerial application operator sets a base price per acre treated by air based on the expected cost of operation. This is the amount he charges the farmer-client. On average, fuel probably accounts for about 20 percent of the total expenses an aerial application business incurs. Depending on the type of fuel an aerial application business uses, of which there are two—avgas for piston engine ag aircraft and Jet A for turbine engine ag aircraft—the aerial application operator includes a base price for fuel going into the season. Some applicators stick with this price regardless of fluctuations in the fuel price and, as a result, may lose money when fuel prices go up steeply. Other small aerial application businesses will incorporate a fuel surcharge into their pricing structure. The decision whether or not to use a surcharge is usually determined by prevalent pricing

practices used in the area by competing businesses – both ground and air. My business will charge a specified dollar fee for each acre I treat for a farmer and that fee ranges depending on whether I am putting out wet, dry or seed materials; if the field is short or long; and other variables. Incorporated within that fee per acre charge, is the fuel charge, which, as stated earlier, is based on an average price of fuel per gallon. This ranges depending on the aerial application operation and the type of fuel used, but, on average it is estimated to be about two dollars per gallon. If fuel rises above that figure—again, each aerial application operation is a little different—a fuel surcharge is added. A typical fuel surcharge is calculated as follows: it is the difference between the average price for a gallon of fuel that an applicator builds into his acre charge and the price of a gallon of aviation fuel at the time of application (assuming that the latter is a greater amount), multiplied by the average number of gallons burned by that particular aircraft in an hour, multiplied by the amount of time it took to make the application for the farmer. For example, if an operator builds a two dollar per gallon of fuel cost average into his acre charge and the price of a gallon at the time of the application is $3.50 the difference is $1.50. If the aircraft being used is a turbine powered Air Tractor AT-502, which burns 50 gallons per hour on average and it takes an hour and a half to fly the farmer client's field then the fuel surcharge would be $112.50.[1]

Based on the higher prices that are being set for agricultural commodities today, fuel surcharges in our industry have been met with minimal complaint by farmer-clients because they will be getting a good price for their crop. This isn't something that aerial applicators are taking for granted, however. According to the USDA's National Agricultural Statistics Service, last month (March 2011), the price of corn was $5.46 per bushel, for wheat it was $7.63 per bushel and for soybeans it was $12.10 per bushel. Because farmers expect to receive a good price on their crop they can absorb the higher fuel prices. If this was 2002 and we were faced with the same high prices for fuel, but agricultural commodity prices were much lower, our industry would be facing some real challenges. According to the National Agricultural Statistics Service, in 2002, corn prices were $2.00 a bushel, wheat prices were $2.80 a

[1]($3.50-$2.00) x 50 x 1.5= $112.50 surcharge

bushel and soybeans were $4.30 a bushel. This is a 273 percent increase in the price for corn, a 273 percent increase for the price of wheat and a 281 percent increase for the price of soybeans in nine years. At the same time the average price of Jet A sold at the retail level from an airport Fixed Base Operator, or FBO, in 2002 was $2.37 a gallon compared to $5.26 a gallon today[2], a 222 percent increase. Typically an aerial applicator will buy fuel at the wholesale level, at a cheaper price than what an FBO will sell, if he is working from his own landing strip but at a public airport he will typically pay the FBO price. As of April 6, 2011 the wholesale price of Jet A without taxes was $3.33 a gallon as quoted by a Southeast U.S. fuel supplier[3]. If in 2002 when commodity prices were much lower and Jet A fuel for turbine powered ag aircraft was the same price today or the same price that it was at its height in 2008 when it averaged $4.72 a gallon, it would be much tougher for a farmer to embrace a fuel surcharge for aerial application services rendered. Realistically, when input prices, such as fuel, are high and commodity prices are low a significant drop in the use of aerial application services and other farm services utilized by a farmer would occur as a result of containing costs. This helps the farmer contain expenses but frequently results in less yield and poorer crop quality, hence negatively affecting his revenue potential. The lack of application is a challenge for an aerial application operator or other farm service provider that requires steady business each season to remain viable.

Another challenge aerial applicators face, particularly when fuel prices are high, is the financial terms that fuel-suppliers have for payment of their fuel and how those terms differ from their own accounts receivable terms. The typical payment terms an aerial applicator has with his fuel supplier is ten days with established credit. If credit has not been established then cash is required at delivery. This usually differs from payment terms that aerial applicators' customers are accustomed to paying,

[2] Nationwide Average Fuel Prices on 4/6/2011 based on prices from 3,602 Fixed Based Operators (FBOs) nationwide according to www.airnav.com. These prices include state and federal taxes.

[3] This price does not include federal excise tax levied on Jet A which is 21.9 cents per gallon; the federal excise tax levied on avgas is 19.3 cents per gallon, and the quote for a gallon of avgas on April 6, 2011 was $3.85 a gallon.

which they would ideally like to be 30 days but typically are between 45-60 days. This can pose challenges because, as stated earlier, fuel costs consist of approximately 20 percent of an aerial applicator's total expenses. Aerial applicators buy fuel by the tanker load or more which is 7,800 gallons. It is not unusual for an aerial applicator to have 10,000 gallons of fuel capacity. With the wholesale price of Jet A today at $3.33 a gallon, a tanker load would run $25,974.00. In 2008 when fuel was at its all time high the price of a tanker load of Jet A at $4.72 a gallon cost $36,816.00. If the average ag aircraft burns 50 gallons an hour and is flown 300 hours a season and there are 2.2 aircraft on average per aerial application operation 36,816 gallons of fuel will be required. When an applicator is facing a 20 to 50 day deficit in accounts payable compared to his accounts receivable and outlaying large chunks of capital for fuel this may result in sizeable interest payments for small aerial application businesses. This condition is only exacerbated when the price of fuel increases which is being anticipated this year. The less burdensome aspect to this currently is that interest rates are low, but as the economy rebounds inflation is anticipated and with inflation comes higher interest rates. That coupled with a greater demand for fuel globally will likely lead to a steady increase in the price of fuel and place much greater cost pressures on small aerial application businesses.

These conditions, in some instances, do lead to aerial applicators taking more risk in trying to hedge the price of fuel. For example, aerial applicators may fill up or top off their fuel tanks during the off season when global fuel consumption is low and they believe the price is below what they will pay in the spring and summer during the busy application season. This doesn't always turn out to be the case, plus the small business aerial applicator is not managing his inventory efficiently by using his off-season cash for fuel rather than to earn interest. In addition, problems can arise from storing fuel for too long of a period, this includes moisture in the fuel, algae problems in Jet-A, and possibly evaporation of avgas. Furthermore, the fuel that can be stored at an aerial application operation, at a maximum, is between one-quarter and one-third of the fuel that the applicator will need for the season. The

remainder will have to be purchased as the tank empties during the application season when the price is higher. Some applicators have even taken on more risk and purchased heating oil contracts on the New York Mercantile Exchange (NYMEX), the commodity futures exchange, as a way to hedge against the high price of fuel similar to how Southwest Airlines hedges its fuel, but the aerial applicator doesn't take delivery of the fuel. The price of heating oil is close to the price of Jet A. Again, this is a riskier way to address the high price of fuel and also requires additional capital outlay, or potentially higher interest costs if purchasing on margin. But to address the high price of fuel, again a considerable expense for small aerial application businesses, different approaches are taken to try to save the farmer-customers' costs and the small business aerial applicators' costs.

One other issue of concern to the agricultural aviation industry that is related to fuel supply and may result in another variable increasing the cost of fuel and/or equipment for our industry is the issue to phase out the use of avgas. EPA is collecting information related to the impact of lead emissions from avgas used in piston engine aircraft on air quality. EPA has mentioned the possibility of a new environmental standard associated with avgas due to its emissions of lead in the air. The FAA General Aviation and Part 135 Activity Survey for the 2008 calendar year indicates that avgas, which is still widely used in piston-powered engines, continues to be used in 51.87 percent or 1,569 agricultural aircraft in the U.S. today. It is safe to say that more than half of the agricultural aviation fleet, and therefore the industry, is still largely dependent on leaded avgas. Environmental groups have rallied behind strict avgas regulations and hope to see avgas phased out completely. Some environmental groups have stated they believe any aircraft using avgas containing lead should be grounded until the appropriate modifications can be made.

NAAA's primary concerns are with the safety and feasibility issues associated with a mandated shift from avgas. Approximately 30 percent of currently registered piston-powered aircraft in the United States could not operate safely on a fuel with a lower octane level than avgas. At this point, no suitable

alternative to avgas exists. Although the automotive industry has been able to move away from leaded fuel and make a shift toward alternative fuels such as ethanol, the same fuel transition cannot be as easily accomplished with aircraft. Ethanol, along with many other alternate fuels, is not suitable for use in aircraft. The Aircraft Owners and Pilots Association (AOPA) noted that adding ethanol to aviation fuel could lead to vapor lock, cause corrosion, possibly introduce water into the fuel system and reduce the energy content of the fuel.

NAAA has urged the EPA to consider the cost burden and overall effect on the aviation industry before imposing any new regulations regarding avgas. NAAA has encouraged the EPA to allow time for and devote resources toward the development of a suitable and sustainable alternative to avgas before imposing avgas regulations or banning use of the fuel. NAAA urged the Agency to consider the detrimental economic impacts that could occur should avgas be phased out prior to the development of a safe and practical alternate fuel. Piston engines are a notably less expensive powerplant for agricultural aircraft and for our smaller aerial application businesses it may be the only type of powerplant that may be affordable. They can be several times less expensive than a turbine engine.

Mr. Tipton, Mr. Critz, thank you for the opportunity for me to express to the Committee the issues affecting the aerial application industry in regards to the supply of fuel prices and the supply of fuel for agricultural aviation aircraft. A national policy that can be developed that would ensure a stable price and supply for Jet A and avgas is imperative for our industry and the farmer clients we treat. Also, a continuation of the fuel tax exemption for aviation fuels used for ag aircraft while flying over the farm has provided some relief to our farmer-customers. Our industry provides a valuable service aiding in the production of the safe, affordable and abundant global supply of food, fiber and bio-fuel. The speed, unobtrusiveness and accessibility of aerial application make it invaluable to agricultural production, forestry production, and public-health pest management. We treat between 200 and 250 million acres

alone in the U.S. each year. As such, a steady supply and price of fuel is vitally important to us and our farmer-customers. Thank you again to you and the members of the Subcommittee.

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Chairman TIPTON. Thank you, Mr. Richter. We appreciate your testimony.

I would like to now introduce Mr. Dick Pingel, who has been an owner-operator trucker for over 28 years, and I also have it on good authority that Mr. Pingel has personally driven over three million miles without a single accident. That is notable. The Subcommittee appreciates you taking the time to speak with us today, Mr. Pingel.

STATEMENT OF DICK PINGEL

Mr. PINGEL. Good morning. My name is Dick Pingel. I live in Plover, Wisconsin, and have been a small business trucker for the past 28 years. I am a member of Owner-Operators Independent Drivers Association and currently run a one-truck operation hauling food around the country.

As you are most likely aware, O-O-I-D-A, or OOIDA as it is known in the trucking industry, is a national trade association representing the interests of small business trucking professionals and professional truck drivers. The more than 152,000 members of OOIDA are small business men and women in all 50 states who collectively own and operate more than 200,000 individual heavy-duty trucks.

The majority of the trucking community in this country is made up of small businesses as 93 percent of all carriers have less than 20 trucks in their fleet and 78 percent of carriers have just 6 or fewer trucks. In fact, a one-truck operation such as me represents nearly half of the total number of federally registered motor carriers. Assuming that the trucking industry exclusively moves about 70 percent of our nation's goods and that just about all freight is moved by truck at some point in the supply chain, it is not hard to see that the costs and burdens that encumber small business truckers have an impact on our nation's businesses and consumers. The cost of fuel is very often the largest operating expense with which small business truckers must contend. For folks like me, fuel costs can easily be 50 percent or more of our annual operating expenses. To give you some perspective, the average OOIDA member runs their truck about 120,000 miles or more each year while getting somewhere in the ballpark of only 7 miles per gallon. Most of us will be operating trucks equipped with either twin 135-gallon tanks or twin 150-gallon tanks, so we can easily see a bill of over 1,000 dollars when we fill up.

In addition to the fuel going into the tanks of my tractor, I use a trailer with a diesel-powered refrigerating unit to haul dairy products for producers in Wisconsin. Until recently, I could count on it costing about $50 to fill up my tank for the reefer unit. However, in recent months the cost to fill this tank has increased to more than $100. The additional money I am now spending on fuel for my truck and trailer once went into investing in other areas of my business, but now it must cover basic operating expenses. Every time I pull into a truck stop I hear similar stories, as truckers are paying significantly more at the pump.

The national average for diesel is now around $4.12 a gallon, with prices in some states approaching $4.50 per gallon. To put this into perspective, each time the price of a gallon of diesel fuel increases by a nickel, a trucker's annual cost increases by $1,000.

Diesel prices today are more than a dollar higher than they were this time last year, resulting in an enormous extra burden on small business truckers whose average annual income is less than $40,000. However, unlike past spikes in fuel prices, the recent increases in the cost of fuel are not occurring in isolation. Over the past few years, the trucking industry has been laboring under a steadily increasing amount of costly and often unnecessary regulations which, when coupled with the rising cost of fuel, are certain to force many small business truckers in very difficult, if not insurmountable economic situations.

Small business truckers operate in a hyper competitive market, so managing their number one expense is imperative for their survival. In our marketplace, we often see costs increase without any corresponding rate increases. As such, the only way to survive is to become more efficient in how one operates their truck. Small business truckers always drive with an eye towards saving fuel no matter what the price because our business survival depends on it. As small business truckers like myself know, reducing fuel costs is not a science, it is an art and one that we pride ourselves on being masters of. However, our ability to practice this is made more difficult by increased regulation and artificially high fuel prices, issues we look forward to working with Congress to address.

Thank you for this opportunity to speak with you, and I look forward to answering any questions that you may have.

[The statement of Dick Pingel follows:]

Testimony of

DICK PINGEL
PROFESSIONAL TRUCK DRIVER AND
MEMBER
OWNER-OPERATOR INDEPENDENT DRIVERS ASSOCIATION

Before the

COMMITTEE ON SMALL BUSINESS, SUBCOMMITTEE ON
AGRICULTURE, ENERGY AND TRADE
US HOUSE OF REPRESENTATIVES

Regarding

DRILLING FOR A SOLUTION: FINDING WAYS TO CURTAIL THE CRUSHING EFFECT OF HIGH GAS PRICES ON SMALL BUSINESS

APRIL 14, 2011

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On behalf of

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Good morning Chairman Tipton, Ranking Member Critz, and distinguished members of the Subcommittee. Thank you for inviting me to testify on matters which are extremely important to our nation's small business trucking professionals and professional truck drivers.

My name is Dick Pingel. I live in the village of Plover, Wisconsin, and have been an owner-operator trucker for the past 28 years. I am a member of OOIDA, and currently run a one truck operation, Finally Trucking Company, hauling food around the country.

As you are most likely aware, OOIDA is is the national trade association representing the interests of independent owner-operators and professional drivers on all issues that affect small-business truckers. The more than 152,000 members of OOIDA are small-business men and women in all 50 states who collectively own and operate more than 200,000 individual heavy-duty trucks.

The majority of the trucking community in this country is made up of small businesses, as 93% of all carriers have less than 20 trucks in their fleet and 78% of carriers have fleets of just 6 or fewer trucks. In fact, one-truck motor carriers represent nearly half of the total number of motor carriers operating in the United States.

I have been asked to come here today to speak on behalf of OOIDA and my fellow professional drivers about the impact that high fuel prices are having on the trucking industry, especially small business truckers like me who personally experience the costs of high fuel prices every day when we fill up our trucks and take to the road. Unlike many industries around the country, the trucking industry is not made up of a small number of major entities who can spread increased fuel costs across their business units; for a large part of the trucking community, when a trucking company pays for fuel, it comes out of the drivers pocket.

Sadly, the impact of fuel prices on the livelihoods of truckers is a story we have told to Capitol Hill many times before. Today, as before, the rising cost of fuel is causing harm to the trucking industry as we know it, especially to small business truckers who are already living load to load. Across this nation, small business truckers are experiencing unprecedented operating cost increases and are being forced to make tough decisions in the name of saving their businesses and providing for their families.

However, unlike past fuel price increases, the recent increases in the costs of fuel are not occurring in isolation. Over the past few years, the trucking industry has been laboring under a steadily increasing amount of safety, security and environmental regulations. While some regulations are necessary to further our overall societal goals, recently, trucking has been assaulted by a barrage of unnecessary and costly regulation which, when coupled with the rising cost of fuel, are certain to force many small business truckers to park their truck.

Just this Monday, diesel's national average jumped to over $4 per gallon for the first time since September 2008, gaining 10.2 cents to $4.078 a gallon, with some drivers in some states seeing fuel prices approaching $4.50 a gallon. To put this into perspective, each time the price of a gallon of diesel fuel increases by a nickel, a trucker's annual costs increase by $1,000. Diesel prices today are around $1 higher than they were this time last year, resulting in an enormous

extra burden on the small business trucker whose average annual income is only approximately $37,000. The urgency for action to help truckers survive grows with every additional cent they must pay at the fuel pump.

On behalf of America's small business truckers, I thank the Subcommittee for this opportunity to highlight some actions that OOIDA feels would address the challenges facing our industry from high fuel prices. We recognize that this problem will not be fixed overnight, but that steps can be taken now that will have a real impact to drivers.

Addressing Fuel Use within the Trucking Industry: Focusing on Real Solutions

Small-business truckers operate in a hyper-competitive market, so managing their number one expense, fuel, is imperative for their survival. In our marketplace, we often see costs increase without any corresponding rate increases; as such, the only way to survive is to become even more efficient in how one operates their truck.

Some have suggested that the best way to address fuel usage within the trucking industry is to adopt technology mandates with an eye towards improving fuel economy. From the perspective of small business truckers, we certainly recognize that many of these new technologies, such as APUs to reducing idling and side skirts to improve trailer aerodynamics, can and do have an impact on improving fuel economy and saving drivers money. However, the use of these technologies must be determined in light of their purchase cost, the fuel savings achieved from their use, and if their installation and use fits with the operating model used by the individual driver and the conditions they operate within.

As professional drivers, OOIDA members recognize that the best fuel saving device on any truck is a well trained and experienced driver. The National Academy of Sciences study titled "*Technologies and Approaches to Reducing the Fuel Consumption of Medium-and-Heavy-Duty Vehicles*" supported this first-hand experience by stating that driver training offers potential savings for the trucking industry rivaling the savings available from technology. The opportunities for fuel savings are significant and indicators are that this could be one of the most cost-effective and best ways to reduce fuel consumption. Professional drivers always drive with an eye towards saving fuel, when fuel prices are high and when they are low because their business survival depends upon it.

However, some are calling for the installation and requirement of technologies within trucks that would only serve to take the fuel saving capabilities of a trained driver out of the equation. Fuel conservation is complicated and can depend on a number of variables including tire pressure, gear ratio, and road conditions. Selling speed limiting devices as a cure all for achieving increased fuel conservation is disingenuous and not supported by any existing real world studies. As professional drivers like myself know, reducing fuel use isn't a science, it is an art, and one that we pride ourselves on being masters at.

Instead of focusing on one-size-fits-all technology mandates, there are significant steps that Congress and the regulatory agencies can take to help small business truckers reduce the cost of operating a truck, including those related to fuel usage, such as the following:

Stop New, Costly Regulations

Over the past 5 months, the trucking industry has had to address 15 new major regulatory rulemakings, almost all of which would add significant costs to truckers while providing limited true public benefit. This comes on top of the additional costs that drivers are paying today for past regulatory efforts. In this context, the impact of today's high fuel costs is clear. By pursuing new regulatory technology mandates, which would create a significant cost for small business truckers, such as electronic on board recorders, speed limiters, and revisions to hours of service regulations, this administration is heaping an unprecedented burden on the small operations who cannot disperse the costs. Small business truckers, who often have decades of experience on the road and are often the ones behind the wheel of the truck with their skin and bones on the line need immediate relief from some of these abusive regulatory pursuits which often serve to only promote large corporate motor carrier interests.

Ensure Drivers Receive Fuel Surcharge Payments

For a wide variety of reasons, owner operators and small business truckers such as myself seldom deal directly with shippers. Most of their freight comes through brokers (third party logistics companies) if they are true independent operations or through a larger trucking company if they are leased as independent contractors. Mid-size trucking firms often have contracts with shippers for 'front hauls', but depend entirely on brokers for 'back hauls'. As I previously mentioned, these small and midsize trucking operations make up the vast majority of the industry. As opposed to large corporations, they are the ones getting particularly hard hit by fuel prices.

Due to the dynamics of the trucking marketplace, truckers are often constrained from adjusting their base freight hauling rates. For many years, the only viable marketplace solution to high or erratic fuel prices has been the application of a surcharge. It is an established means by which trucking companies are able to vary their pricing to respond to higher or lower fuel costs. With diesel prices consistently rising, shippers are paying more now in fuel surcharges to get their freight moved than ever before. Unfortunately, all too often motor carriers and transportation brokers push shippers to pay higher fuel surcharges, but may pass along only a portion, or sometimes nothing at all, of those surcharges to the truckers who are actually hauling the freight and paying the fuel bill. Congress or appropriate Executive Branch departments should act to address this issue and ensure that fuel surcharges paid by shippers are being passed along in full to the individuals who pay for the fuel to haul those shippers' freight.

Address Excessive Detention Time

Shippers and receivers routinely make truckers wait for considerable amounts of time before they allow them to load or unload their trucks. Drivers, including myself, routinely arrive at loading facilities with little or no idea how long they will be there. When detained while delivering refrigerated freight, my refrigeration unit must run the entire time I am waiting, wasting fuel while I await my turn at the dock.

Known in the industry as "detention time," most shippers do not pay for this time and have little financial or regulatory incentive to make more efficient use of drivers' time or fuel. It is common for a driver to pull into a shipping or receiving facility and wait for 2 hours or for 10, in many

cases using fuel. Reasonably addressing detention time, either through limits or guaranteed detention pay, would truly reflect the cost of detention on the supply chain, including the increased use of fuel during these periods.

Advancing Driver Training

As noted above, putting well trained drivers behind the wheel is the number one way the trucking community can reduce its fuel use. To this end, OOIDA and its membership of professional drivers has consistently been a strong proponent of Federal efforts to develop and impose mandatory, comprehensive driver training and licensing requirements for entry-level truck drivers.

At present, FMCSA regulations require entry-level drivers to be trained in only four subjects – driver qualifications, hours-of-service, driver wellness and whistle blower protection – all of them unrelated to the hands on operation of a commercial motor vehicle. In 2008, FMCSA moved forward with the first step in issuing regulations that would expand the required training for Class A drivers to include a minimum of 44 hours behind the wheel training in addition to 76 hours of classroom training. While nearly all of this training will pertain directly to the operation of a commercial motor vehicle, little to no time will be spent focusing on fuel efficient driving techniques. OOIDA feels that the required training is a unique opportunity to instill these strategies with new drivers, and calls upon FMCSA to expand their proposal to cover this important area of commercial motor vehicle operation.

Domestic Energy Resources: Increasing Production to Mitigate Price Spikes

Like all businesses, small business truckers prefer predictability. They like to have predictable loads, predictable weather conditions and traffic, and most of all, predictable fuel prices. During these times of predictability, we are able to manage our businesses in a way that positions us for future growth, benefiting the overall economy.

Today, as in 2008, we are now forced to manage for survival, as fuel cost increases have a direct impact on our bottom line. While most discussions of fuel costs on the trucking industry rightfully focus on the tractor, these increases have wide standing impacts. Let me use my own experience to illustrate. I use a refrigerated van to haul food products, especially dairy products from Wisconsin producers, and my refrigeration unit uses diesel to operate. Since the last price spike, I could count on the tank for the "reefer" costing about $50 to fill up; however, in recent months the cost to fill this tank up has increased to $100. The $50 that I am now spending on this necessary part of my business once went to investing in other areas, but that now has stopped.

The impact that these price spikes have on the small business trucker are devastating, halting investment and potentially forcing drivers to default on the loans that finance their trucks. In the past, domestic energy production has helped mitigate price spikes based on international conditions, but the limitations on production currently in place have helped pass along to truckers the energy price increases related to unrest in the Middle East far more quickly than in the past. There can be no doubt that the fuel prices truckers pay today are dramatically impacted by speculation in the petroleum markets. When a potential supply disruption occurs thousands of miles away and results in a price change in truck stops across the country that very same day,

there is a level of volatility in the market that is not connected to any true measure of energy supply.

OOIDA and its members support efforts to expand energy production here at home, from the Gulf of Mexico to the new oil-shale opportunities in the West and urges Congress and the Administration to take actions to proceed with new developments and to restart exploration and production operations currently under constraint. This is especially true of areas in the Gulf and of the area off the shore of Virginia that have seen their leases canceled or delayed. It is difficult for truckers to understand why there will be no new offshore lease sales this year, the first time that has occurred since 1958, when fuel prices are this high.

Additionally, there needs to be action to reduce the regulatory challenges faced by producers as they look to locate and develop new sources of energy. These regulatory challenges, including significant overlaps in agency responsibility, are especially difficult for small energy producers to navigate. Much like the small business truckers I am here speaking on behalf of, these small producers often operate drilling lease to drilling lease and do not have large international operations to leverage against should government delays slow down their progress. In containing the reforms to the Department of the Interior's energy development process, Congress and the Administration should focus on ensuring that regulatory requirements will achieve their desired intent and not simply add new requirements to industry for the sake of adding requirements. We in the trucking industry have experienced such actions first hand, so we speak from experience.

Conclusion

Mr. Chairman and members of the Subcommittee, I thank you again for the opportunity to testify today. If there is any industry that reflects the small business heart of this nation, it is the trucking industry and the community of small business owner-operators that make up its core.

As professional drivers, we see the impact of high fuel prices every day, and we understand what it takes to control fuel usage. Unfortunately, today's high fuel costs are only adding to the challenges imposed upon the industry from numerous, costly government regulations. We look forward to working with this Subcommittee and the entire Congress to find solutions to address our nation's energy challenges while ensuring that regulation of our industry is focused on promoting safety, not simply mandating one-size-fits-all technologies.

Chairman TIPTON. Thank you very much, Mr. Pingel. I appreciate that. And I would now like to yield to Ranking Member Critz, who will be introducing our next witness.

Mr. CRITZ. Dr. Robert Weiner is a professor at George Washington University. Professor Weiner has authored or co-authored four books on energy markets and oil. He has also authored more than 50 articles on environmental and natural resource economics focusing on energy security, risk management, and the oil and gas markets and companies. Professor Weiner's current research interests include financial innovation and commodity markets, oil and gas trading, and risk management in the oil and gas industry.

He received his Ph.D. in 1986 from Harvard University and has been at George Washington since 1994 serving as chairman of the International Business Department from 2001 to 2005. He is currently associate director of the Global and Entrepreneurial Finance Research Institute at George Washington. Dr. Weiner.

STATEMENT OF ROBERT WEINER

Mr. WEINER. Mr. Chairman, Ranking Member, other members, thank you very much for the opportunity to be here. I would like to say that I am not representing anyone except for myself as a student of the industry.

What I would like to do is divide my remarks into three parts. First, where prices are and where they are going and the implication for small business; second, political risk and the impact of political risk, including political risk in the United States on investment in the oil industry, oil production, and eventually prices; and third, time permitting, the causes of the underlying increase in oil prices.

First, the key question for everyone especially for small business, is how to adapt to higher and more volatile prices. In order to figure this out we have to get a sense of where prices are going and also where they are likely to be in the future in an industry in the United States that produces over 5 million barrels a day. The average well produces 10 barrels a day. So I would like to remind people here that the small business that we discuss includes the oil industry. There are many small businesses in the oil industry, both in conventional oil but also in the newly emerging technologies that will be important in the future, such as shale and services for deepwater exploration.

In order to look at forecasts, we need to get a sense of what the market thinks. I am not a forecaster but I am a consumer of oil price forecasts, and the advantage of the market forecasts are three. The first is that they are widely available, and like some of the best things in life they are actually free. You do not have to pay for them. Second is they reflect the consensus of many, many small buyers and sellers in the market, putting their own capital at risk and their clients' capital, and they will lose if their forecasts are wrong. And then finally, the tendency of these forecasts to be right on average. In other words, these forecasts are on bias. Whatever the forecast is for the end of the year, which is about $105 a barrel, the chances are equal that it will be too high and too low.

What the forecast tells us is four things. First, that people expect the price increase to be permanent, where permanent in my world

means six or seven years. The futures price for the end of 2016 is $105 a barrel, only slightly below today's $110 a barrel. And, of course, future price expectations include expectations about the deliberations of this August body in terms of the ability of the U.S. or the lack of the ability of the U.S. to increase production. And so that skepticism or concern is inherent in prices.

Second is prices are expected to stay high but to plateau. No future increase in prices unless there are some political events that are hard to predict such as those in Libya or Japan or indeed in the Gulf of Mexico.

The idea of peak oil, which is the third idea, is simply not supported by expected prices. Peak oil suggests we are running out of oil. I think we have seen the entrepreneurship and the ingenuity and technology of business in the United States. The ability to, at least for now, stay well ahead of the battle against depletion and to be able to increase, if allowed, by regulation our domestic energy production.

And finally, there is no intrinsic value for oil. All of us who may have hoped that just because prices are higher than historically now means that they will go back to previous levels, the forecast says that they will not. The new normal is that there is no normal.

Because I am running out of time I would like to switch to talk about political risk. Political risk restricts investment at all levels. Political risk is not something that we think about just for a country like Libya or Iraq. Political risk is very much present in the U.S., especially in the deepwater Gulf of Mexico and in shale because of uncertainties about environmental effects and difficulties of the industry in getting permits and permission to drill. Right now an enormous amount of industry capital is tied up essentially doing nothing or very little, wondering when permits will be issued. The industry has long been able to deal with regulation and taxes as long as it is clear. As the president of Exxon said a few days ago, the U.S. is a very difficult country to do business right now. Political risk means it is hard to figure out whether the industry should invest. Without more investment there will not be more production, and without more production there can only be higher prices.

I see that I am out of time so I will reserve the rest of my remarks for my written testimony. Thank you very much.

[The statement of Robert Weiner follows:]

Recent Oil-Market Developments: Causes and Implications

Statement of
Professor Robert J. Weiner
Professor of International Business, Public Policy & Public Administration,
and International Affairs,
George Washington University

before the
Committee on Small Business
Subcommittee on Agriculture, Energy, and Trade
United States House of Representatives
April 14, 2011

My name is Robert Weiner. I am Professor of International Business, Public Policy & Public Administration, and International Affairs, George Washington University, in Washington, D.C. I am also affiliated with a couple of small business, one in consulting, the other in financial services. It is an honor and a privilege to be here today and to offer observations about developments in the world oil market. My views are my own, based on three decades of studying and writing about petroleum. I am not appearing on behalf of my employer or any other entity.

The past few years have witnessed unprecedented volatility in oil and gas markets. The price of a barrel of crude oil has vaulted from a low of $10 in the late 1990s to almost $150 in Summer 2008. By December 2008, prices had plunged to $30 per barrel, only to climb back over $110 Friday April 8, 2011. Natural gas prices have been just as volatile, rising to over $13/MMBTU (million British thermal units) in the USA in 2008 before falling back to less than $2 in Fall 2009, over $7 in early 2010, back to about $4 Friday.

This volatility and the causes behind it have been a source of concern to policy makers, industry, and civil society worldwide. How can a commodity so central to modern life be so volatile? What are the reasons behind high and volatile prices? Will this volatility continue? Can it be managed? What are the implications for business?

We all would like to know how long current high oil prices will last. While nobody can foresee the future accurately, "reading the tea leaves" can take us surprisingly far –petroleum futures markets can provide a quick, cheap and unbiased forecast of future oil and gas prices. The lines in Figure 1 below show market forecasts on the dates indicated. When the spot price reached $90/barrel at the end of 2010, the forecast for the end of 2016 was also $90. When the spot price reached $110 last week, the forecast for 2016 was $105. ***In other words, the market expects most of the current dramatic elevation in oil prices to be permanent.***

To make sense of this, we need to understand what a market forecast is, and how accurate it is. The market forecast presents the consensus of people willing to commit their own and their clients' capital in buying and selling oil for future delivery. Forecasts are not made

lightly, and have financial consequences for those acting on them. A backward look at past forecasts shows that they are unbiased, meaning half the time too high, half too low, but correct on average. They are not very precise, however, regularly turning out way too high or way too low. They are the best guess we have, however.

This "best guess" has several implications:

- Prices are not expected to stabilize, not continue climbing, as in Dec. 2008. An extreme view that the world is "running out", sometimes called "peak oil," is not supported by the data. Sheikh Yamani (former Saudi oil minister) said it best:

  "The Stone Age did not come to an end because we had a lack of stones, and the oil age will not come to an end because we have a lack of oil."

- There is no "true value" or "the price" of oil. Some analysts claim "commodity cycles" – when prices are high they end to return to earth, when low they bounce back. In fact, the opposite is the case; oil prices are close to a "random walk."

- High prices are likely here to stay, so need to adapt. Small business in most countries is accustomed to much higher prices than in the US as result of high taxes. For example, in the UK, gasoline prices are the equivalent of $10/gallon.

Some observer are leery of forecasts based on futures markets, and are more familiar and more comfortable with reading tea leaves from the stock market. ***In 2011, the stock-market forecast tells a similar story***. The price of BPT, a royalty trust traded on the New York Stock Exchange, reflects market expectations of oil prices over 15 to 20 years, and has risen sharply after a period of low volatility.

Figure 1: Recent WTI Crude Oil Spot and Futures Prices

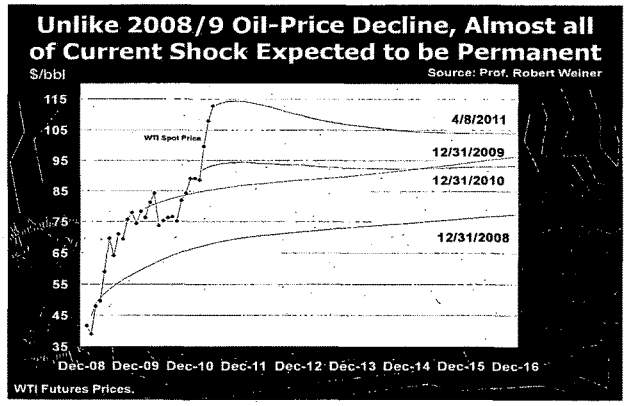
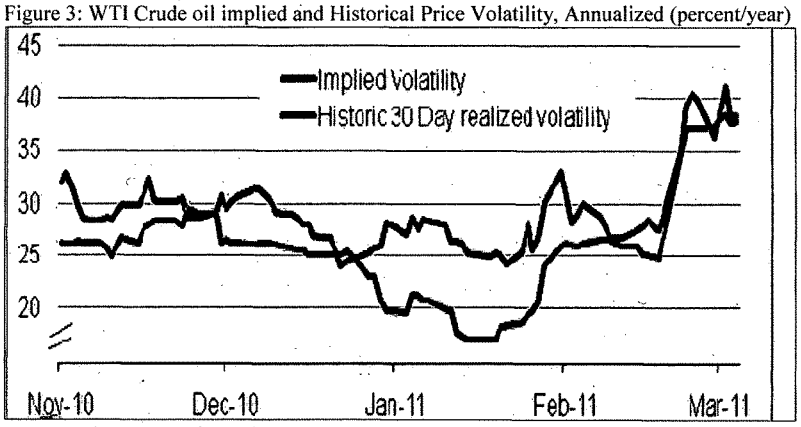


Figure 2: Stock-market Indicator of Long-Term Oil Price Expectations

Market expectations of future volatility have also increased. As seen below, the distribution of likely future prices has widened, reflecting increased uncertainty. Market assessment of future volatility is implicit in options prices. The market forecast of volatility can be imputed from the prices of traded options, and is called ***implied volatility***.

Figure 3: WTI Crude oil implied and Historical Price Volatility, Annualized (percent/year)



Source: US Energy Information Administration

Volatility matters a great deal to the oil industry and the economy, especially to credit-constrained participants, such as small businesses, and governments of many oil-exporting and oil-importing regions and countries Is this volatility likely to continue? A ***yes*** answer would have very different implications than a ***no*** answer for financial management, investment, and economic stability.

Addressing this question requires understanding and assessment of the underlying ***causes*** of volatility. To gauge whether oil prices are likely to be high and volatile in the future, it is necessary to understand why they are where they are today.

There are three potential types of factors underlying volatility. First is market fundamentals — supply, demand, and market power; second is speculation second; and third is market manipulation. In a market as large as international oil, the last is relevant only over very brief periods, and cannot be behind the price trends of the last year.

The "fundamentals view" emphasizes increasing scarcity of petroleum as a nonrenewable resource. Fundamentals refer to consumption changes stemming from economic growth in China, India, and other countries, as well as supply changes associated with depletion of low-cost sources of supply, and the absence of discovery of new large oil and gas fields. These changes are seen as the main drivers behind increasing oil prices. Figures 4a and 4b below show that almost all of the increase in oil demand in the past decade is from developing countries. Figure 4c focuses on China; the country still uses far less oil that the USA.

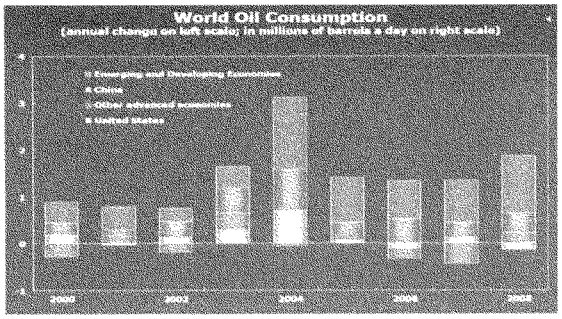
In this view, long-term changes in production and consumption are overlaid with short-term fluctuations in fundamentals arising from weather, natural disasters, conflict in oil-exporting countries, and unpredictable production decisions by the Organization of Petroleum Exporting Countries (OPEC).

An alternative view is that higher prices may be due to fundamentals, but that speculators (traders from outside the oil industry seeking gains from price fluctuations) are behind volatility in these markets. Speculative activity in oil and other commodities is climbing rapidly with the expansion of hedge funds. Moreover, pension funds and other investors are sinking more capital into commodities, including oil. Suspicion about speculative activity is fueled by the absence of comprehensive data on the extent of speculation around the world.

It is common during times of market upheaval, however, for policy makers, industry, and civil society to place much of the responsibility on speculation. Speculative capital has been characterized as "hot money," with capital flows driven by "herding" and "contagion" among participants in foreign-exchange, stock, bond, and commodity markets.

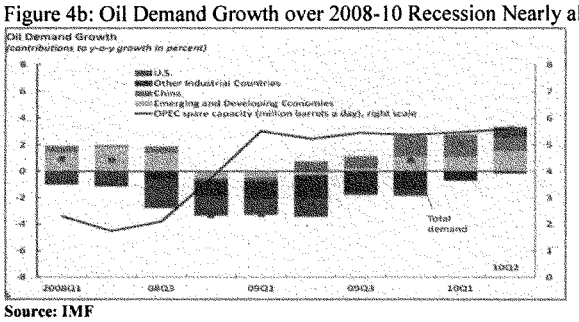
In the case of oil markets, research by others and myself casts doubt on the role of speculators in oil-price volaitltiy. On any given day, roughly half the speculative action is on each side of ht market, leaving little room for speculators to influence oil prices over horizons longer than a couple of days. See e.g., Weiner, "Sheep in wolves' clothing? Speculators and price volatility in petroleum futures," *Quarterly Review of Economics and Finance* 2002, http://www.sciencedirect.com/science/article/B6W5X-45MW05T-D/2/3fe7531fbbfdb448be452c5d1e7b6107

Figure 4a: Oil Demand Increases over 2000-2008 Nearly all from Developing Countries



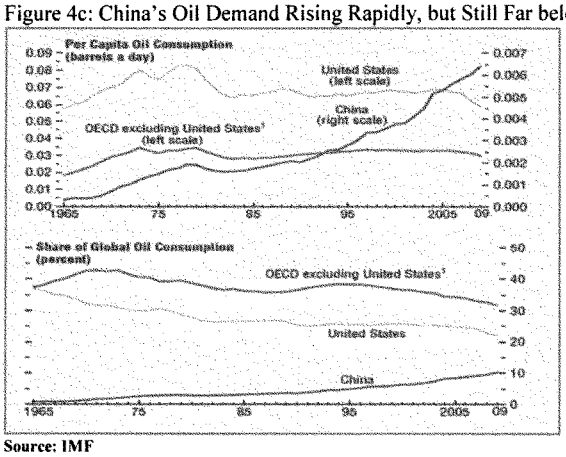
Source: IMF

Figure 4b: Oil Demand Growth over 2008-10 Recession Nearly all from Developing Countries



Source: IMF

Figure 4c: China's Oil Demand Rising Rapidly, but Still Far below Industrialized Countries'



Source: IMF

and Weiner, "Speculation in international crises: report from the Gulf," *Journal of International Business Studies,* 2005, http://www.palgrave-journals.com/jibs/journal/v36/n5/abs/8400158a.html

If speculators do not affect oil prices much, what does? Volatility may be a cause of the dramatic increase in speculative oil trading, but it is unlikely to be an effect. Instead, volatility is related to shocks to oil supply and demand stemming from factors like geopolitics, weather, and economic growth. As oil production declines in the US and North Sea (Figure 5a), the demand increases above are being met from production from countries of the former Soviet Union and OPEC (Figure 5b). Over three-fourths of the world's oil reserves are concentrated in OPEC (Figure 5c). Worldwide, a handful of countries amount for most oil reserves (Figure 5d).

Figure 5a. US and North Sea Oil Production Declining

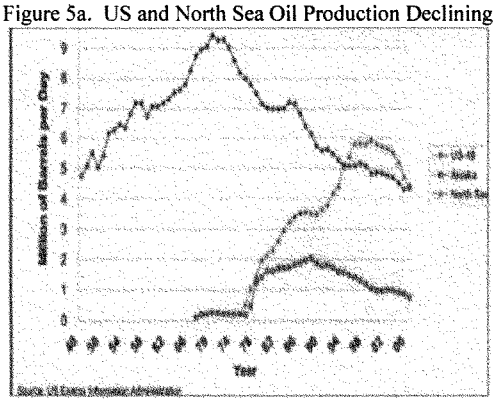
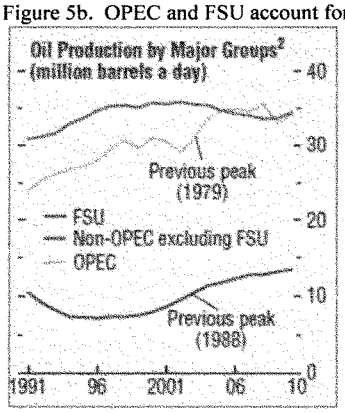


Figure 5b. OPEC and FSU account for All of Oil Production Increase over last Decade



Source: IMF

Figure 5c. OPEC dominates world's Oil reserves; a few countries dominate OPEC

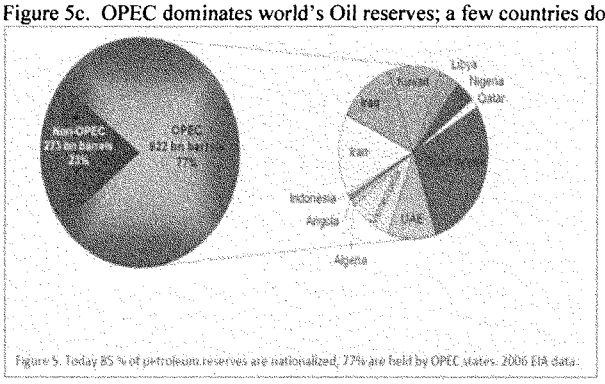
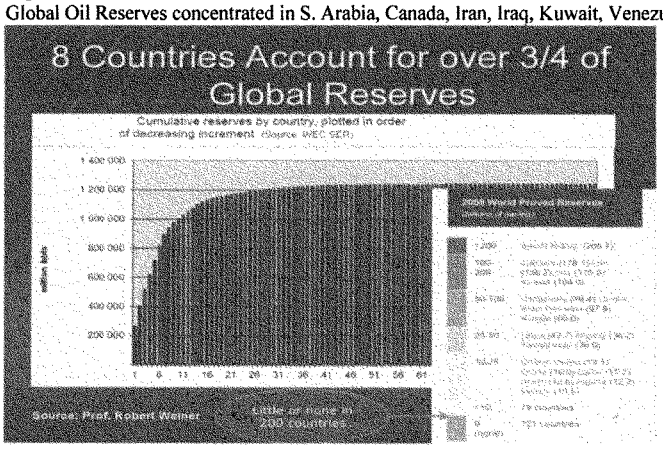


Figure 5d
Global Oil Reserves concentrated in S. Arabia, Canada, Iran, Iraq, Kuwait, Venezuela, UAE, Russia



Policy risk in the USA and Other Countries Destroys Asset Value, Hurting Investment and Future Production

While there may be little that US businesses can do about market volatility beyond managing risk, the country can promote investment, and eventually additional production, through reducing non-mark volatility, especially policy volatility. Political risk reduces investment and destroys the value of petroleum assets. While political risk is clear in countries such as Russia, Venezuela, and Libya it is also an important factor holding back investment and future production in almost every oil-producing country, including the USA (Figure 6).

Figure 6. Policy risk is a factor in almost every oil-producing country, hurting investment

Recent Examples of Policy Risk in Industrialized Oil Countries

- The current (March 2011) UK Budget raises taxes on domestic oil-production income from 50 to 62 percent. ***"Valuations of U.K. assets have been lowered by 15 to 20 percent,"*** *said an analyst at RBC Capital Markets in Edinburgh. "The rate rise is particularly unfortunate for potential sellers of North Sea assets."* **Businessweek,** 25 March 2011
- Following the 2010 Deepwater Horizon Spill, the US federal Government froze drilling offshore Alaska and Gulf of Mexico, idling (domestic and foreign) investment. ***"Political risk in the US is very high.*** *Not just for our industry, but for business in general. Managing our risk here is a significant undertaking, just as it is in many other parts of the world.* ***This is not a particularly easy place to do business in."*** Exxon CEO Rex Tillerson, interview published 11 April 2011
- The Alberta government hiked gas royalties in 2007, but **reversed the changes in 2010 as investment left the province.**

Conclusion

The long-run level of oil-price volatility is high, and likely to remain high. The fundamental factors driving volatility show no evidence of increased stability. On the other hand, signs of continuing increases in volatility are also few. The world economy is likely to face volatility levels similar to those in the present and recent past for an extended period. Like many markets, oil has experienced periods of extreme turbulence (sometimes called "shocks" or "disruptions"), which will likely continue. Volatility could easily be substantially elevated over long-run levels for limited periods.

Business will continue to be innovative and adaptable in a world of high and volatile oil prices. To foster investment and future production, it is important to establish and implement clear, stable policy in the areas that affect petroleum the most – taxes and regulation. This is most easily seen for offshore drilling, but also affects new technologies (e.g., oil and gas production from shale).

Chairman TIPTON. Thank you Dr. Weiner. We certainly appreciate your testimony and paying attention to the lights, too. We often ignore them up here.

I appreciate all of you gentlemen taking the time for being able to join us today and I will start out our questioning here. And I would like to start out with my constituent, Jim Ehrlich.

Jim, I do not think that Americans truly realize the significant amount of energy that is necessary to be able to produce food stuffs in our country that we eat daily. Given that upwards of 50 percent of total production expenses are reliant upon energy costs as you noted in your testimony, do you believe that if oil prices reach or exceed, and they already have now, the 2008 gas price level of $4 a gallon that it will force potato farmers out of business or force them to make substantial cutbacks?

Mr. EHRLICH. Well, I think that they will definitely have to cut back but I think the key to that is the price of potatoes. This year the price of potatoes is quite high, as all commodity prices are. As a matter of fact, a lot of commodity prices are at all-time highs. Whether that is sustainable, history would tell us no. So I would say that they will definitely be hurt. If potato prices go back to last year's levels, it will force producers out of production.

Chairman TIPTON. Well, I thought it was worthy of note in your testimony you were talking about the domino effect. If the potato farmer is not doing well, essentially you were noting that the person who operates the local theatre or the local drive-in is going to be impacted as well. Are you seeing that as well in our rural communities?

Mr. EHRLICH. Well, I would say since the economy had the downturn, our area of the country has suffered. And it was not—it did not happen rapidly in agricultural rural areas like that, sometimes the effect happens a little later. But I would say we are actually—we are not out of a recession in the area that I live in. And if the farmers are the only ones making money down there right now, this rise in fuel prices will definitely have a detrimental effect on our area.

Chairman TIPTON. Great. Thanks, Jim.

Dr. Weiner, as you know, President Obama's 2012 budget included roughly $90 billion on taxes on the energy industry. Given your testimony that you just presented, do you believe that implementing more stringent tax policies on energy producers will contribute to higher prices at the pump?

Mr. WEINER. I think it will but I think what is most important is that the energy producers know what the taxes are. I think the thing that is most difficult is when they do not. And one important aspect of higher taxes and tax uncertainty is value destruction. In the current budget for the U.K. that was just released a couple of weeks ago there was a sharp rise on taxes proposed for U.K. and foreign oil producers. The immediate effect was a 15 to 20 percent destruction of value of those investments. So these taxes go right to the bottom line and where there is destruction in value of the asset, of course there will be less investment and eventually less production and higher prices.

Chairman TIPTON. Great. Thank you.

Mr. Richter, in your testimony you pointed out that potential EPA regulations on avgas, which is still being used by the majority of agricultural aviators, you noted that there is no viable alternative right now for avgas. If gas restrictions are put into place, would this effectively close a lot of our sprayers?

Mr. RICHTER. Mr. Chairman, yes, it would. It would definitely close some of the smaller businesses that are using piston-engine aircraft. What you have got to understand is that the larger turbine aircraft are several times more expensive than the smaller ones, and if it would restrict or if there is a ban completely on avgas you would see probably some of those going out of business because small businesses could not afford the larger turbine aircraft. And it would eventually have an effect on food prices in the end.

Chairman TIPTON. Great. Mr. Pingel, you indicated that over the last five months, 15 new major regulatory rulemaking proposals were proposed on the trucking industry. Can you highlight some of the most significant new regulations that you are seeing come out?

Mr. PINGEL. Well, we have seen laws come out at FMCSA on onboard recorders, on speed limiters, on cell phone use. We have seen, not so much in the last five months but in the last few years, 07–10, we have had EPA regulations coming out for emissions on the trucks and those have all, you know, we have had to pay for those.

Chairman TIPTON. Just kind of curious. You know, in your commentary that is over and above when you noted that for every nickel increase in a gallon of gasoline that is a thousand dollars a month if I recall correctly or $1,000 annually in terms of cost.

Mr. PINGEL. Annually.

Chairman TIPTON. These are for independent small business people earning $40,000 a year?

Mr. PINGEL. Correct. And that comes off the bottom line.

Chairman TIPTON. So the increased regulations that we are seeing are hurting small businesses, costing consumers more, and hurting the American economy?

Mr. PINGEL. Correct.

Chairman TIPTON. Thank you so much. I appreciate that. I would like to now yield to Ranking Member Critz for questioning of the witnesses.

Mr. CRITZ. Thank you, Mr. Chairman. You know, what is interesting about these hearings is that usually we come with prepared questions and then as we listen, all these other questions come to light that we want to ask. And Mr. Ehrlich, you had mentioned about in your area the downturn in the economy usually hits slower and it stays longer. I am from rural Pennsylvania and it is usually an indicator in most rural indicators that it takes longer for recessions to hit but it usually hangs on longer and it takes our areas longer to recover as well. And although our hearing is about gas prices, you hit on something that is really a sore spot for me as well.

And actually, my question is going to be to Dr. Weiner, is that EPA regulations—and you know, we did just take the vote on the NPDES—but you had mentioned, Dr. Weiner, about EPA regulations and the need for stability and ways for companies, whether

they be oil, gas, or any company, to be able to plan based on what a stable environment looks like in the future. And I am curious if you can, although it is sort of off the track of gasoline, if you could comment on some of the actions currently that are going on at EPA, what you see, and what the future looks like and what we need to do up here at the congressional level to try to create that stable playing field for industry.

Mr. WEINER. I apologize, Congressman, I am not an expert on EPA at all. I know more about energy than the environment.

I think in general when you are looking at regulations, some regulations affect the bottom line of producing companies a lot more than others. Those are the ones where stability and certainty are really the most important. And there may be a lot of regulations and some of them may be irrelevant or a nuisance but they may not have as big an effect on the bottom line. The question is where does it—where does the buck stop? That's when the question about whether it affects people's decision on investment. The little description that I gave you about the increase in taxes which is just as important for stability in the North Sea, the first thing that happened is some of the companies said we are reassessing because these are high cost fuels to produce. We may not be investing anything. If they do not invest, no production. And no production simply means that more and more of our oil is going to come from places like Venezuela and Iraq and places that we have come to depend on.

Mr. CRITZ. Okay. And I think it is that stability. You mentioned at some point there is a whole lot of people sitting around waiting for permits and different things which means there is no production going on. And like I said, that is sort of a sore spot for me. And when you mentioned the EPA and NPDES and you mentioned it, I thought, sorry, I have got to veer off here because I have got a thorn in my side and I am trying to extract it.

Mr. Pingel, I have one question for you that, again, it is about gas prices but it is also about infrastructure. Is that there is a debate going on about—and actually this could be for anyone who wants to comment—a debate going on about highway—the reauthorization of the highway bill and what it means to infrastructure, building our infrastructure. And we have a huge issue because of lack of money in the Highway Trust Fund to do a lot of these projects. So there is a lot of debate going back and forth on increasing a gas tax. And, of course, in our neck of the woods that is, you know, talking about increasing taxes is nothing that anybody ever wants to talk about but when you are talking about infrastructure sometimes you have to have a tough nut to swallow.

I would be curious what your thoughts are being in the trucking industry you are on the highways all the time, and actually in aviation as well. What that means, you know, what the lack of a highway bill means to you folks.

Mr. PINGEL. Well, I think as far as the gas tax, we realize, the industry realizes that we have to pay for the infrastructure and we know that it is crumbling. But we also see that if we can improve the infrastructure, we can save ourselves money and congestion and, you know, wear and tear on equipment. It is just a matter of taking that money, you know, that we pay in and using it for infra-

structure, not for high-speed rail and bullet trains and bike paths and some of the other stuff. I mean, as an industry, I mean, like I said, we realize that we use it probably more than anybody else and we are willing to pay for it but we want that money to stay where it goes.

Mr. CRITZ. Right. Right. Okay. Any comment, Mr. Richter?

Mr. RICHTER. I might add that many of the agricultural operations, aviation operations, occur on airstrips that are not improved. They are on private airstrips. And we are very fortunate to have a fuel tax exemption. And that has been real good for our industry. It has served us very well. But as such, we rarely use improved airstrips.

Mr. CRITZ. Okay. Well, I appreciate that.

Mr. Chairman, I have about a thousand questions but in the interest of time I will yield to other members of the Committee so that they can ask their questions and on the second round we will come back around. Thank you very much.

Chairman TIPTON. Thank you, Member Critz. And I would now like to recognize Congressman Fleischmann.

Mr. FLEISCHMANN. Mr. Chairman, Ranking Member, thank you very much.

Gentlemen, this is outstanding. I have really enjoyed this testimony so far. It is very helpful.

My name is Chuck Fleischmann. I represent the 3rd District of Tennessee. In addition to serving with the chairman on this Committee, I serve on the Committee of Natural Resources, Energy, and Minerals Subcommittee with my distinguished colleague, Mr. Landry. I am also on the Small Business Committee, so this has really brought my three disciplines together and I have enjoyed this very much and I thank you.

Dr. Weiner, I appreciate your comments on this and I listened very, very intently. One of my goals and one of my passions is to encourage the development of our natural resources in this country—coal, oil, natural gas. I think we have got the domestic resources, particularly the oil, to go out and harvest and develop it. When we were talking, and I appreciate your discussion about value destruction and the like, we were talking about taxes. I am generally adverse to taxes. Okay? Overwhelming. But with the Obama administration's proposed taxes on the oil industry, I think that would be viewed more as a deterrent. You mentioned the term about predictability. What would be the best thing in your view to get the industry to be more attractive as an investment to go out and to develop our oil resources?

Mr. WEINER. Congressman, I think you make some very good points. I think the single most important thing is access and stability about access. Right now people who have invested hundreds of millions in heavy equipment in the Gulf of Mexico are watching their equipment stay idle. Of course, that is costing a lot of money. People are uncertain about the ability to lease things, both on land and offshore. Uncertainty about environmental treatments. And so one of the questions about shale gas which extends to your state as well is about the ability to exploit shale gas given environmental uncertainties.

Resolution of uncertainty is very important. Just like the trucking industry, the oil industry can live with taxes as long as the industry knows what the taxes are. And when you get a lot of uncertainty and flipping back and forth in policy, people in the industry do not know what to do. That is where the value destruction comes. If you cannot exploit the asset, as you mentioned the natural resources, it is just lying idle it is not contributing any value to society.

Mr. FLEISCHMANN. Okay, thank you. Dr. Weiner, I wanted to ask you something about the permitting process. It seems to have been impeded greatly by this administration. Have you delved into that and ways it perhaps could be alleviated so that we could get more permits so that we could actually go about recovering our resources? As you say, these people have got the rates and the machines ready to go but they cannot get the permits at a rapid enough pace. It has been impeded greatly until lately. They just recently eased up. Do you have any thoughts about that, sir?

Mr. WEINER. Very important question, Congressman. The big change has been the change in regulations associated with the Deepwater Horizon accident from exactly a year ago. The procedures have changed and, therefore, the review process changed and the Bureau of Ocean Energy Management that does this permitting does not have much of a staff. And so unless you guys see it appropriate to give them the resources that they need it will be hard for them to get more permits. They have a very small number of staff members for a lot of ocean out there, so one of the things you have got to do is give them the resources and the industry, like the trucking industry, has a good return on capital and would much, much prefer having a stable process where they know they can get their permit process as opposed to just sitting on someone's desk. That is much more important than just having lower taxes.

Mr. FLEISCHMANN. Thank you, Dr. Weiner. Thank you, gentlemen. I yield back, Mr. Chairman.

Chairman TIPTON. Thank you, Congressman Fleischmann. I would now like to introduce Congressman Landry for questioning.

Mr. LANDRY. Mr. Chairman, I have got to tell you I cannot thank you enough for bringing Professor Weiner here. I am going to work on trying to get you in front of the Natural Resources Committee. Your testimony today has been enlightening in an argument that we have been making for the past month and a half in that committee.

But I want to make sure that what I am hearing is correct. We have the ability or do you believe that we have the ability that an increase in production in this country of oil has the ability to affect the price?

Mr. WEINER. Yes, Congressman, it does.

Mr. LANDRY. Thank you. Thank you.

The other question—and of course I represent the 3rd District of Louisiana which is along the coast. All that idle iron that you are talking about, all of those hundreds of million dollars in investment of my constituents and my business owners that are reeling from this de facto moratorium and the policies that this administration is putting on us. One of the things that I found amazing is that the price of natural gas seems to have stabilized over the course

of, I would guess, the last 24 to maybe 36 months. Would that be a correct statement?

Mr. WEINER. Yes, you are seeing the effects already of the shale gas investment and the shale gas production. Shale gas has come online much earlier than people expected and so now you have a disconnect where gas is much less expensive relative to oil than in the past. And I think one of the opening remarks of one of your colleagues said the U.S. has the capability in a few years to be actually an exporter of gas which would help our country in a number of different ways.

Mr. LANDRY. Would you say that prior to that trend oil and natural gas, that prices moved in cadence from peaks and valleys when you look at the graph, I guess, in the last 30—other than say from 2008, I guess, from the time the shale plays were put into play, but prior to that that oil and gas basically moved in cadence? When oil was up, gas was up.

Mr. WEINER. That was true most of the time because gas has a restricted transportation system. When you have something like a freeze in the central part of the country where you cannot get more gas in there you sometimes had these peaks and spikes in natural gas prices that you did not see in oil, especially in the cold winter. But your statement is true, over the longer term they tended to move together.

Mr. LANDRY. Now, when they move together, I am just curious, I do not know the answer to that but when they move together, we were still importing a tremendous amount of our oil but we were not importing a lot of natural gas. Was it just that oil drew gas up or was it truly a supply and demand issue?

Mr. WEINER. Well, Congressman, I believe that everything is truly a supply and demand issue.

Mr. LANDRY. Me, too. I am confused by it.

Mr. WEINER. The U.S. imported about 10 to 15 percent of our natural gas needs so we were importing primarily from Canada, but also liquefied natural gas to Louisiana and other places. Oil and gas—oil is priced in a world market so we have an influence. If we produce more, that will put downward pressure on oil prices; if we produce less, it will put upward pressure on oil prices. Natural gas is more of a local or regional phenomenon, so it tends to track oil but not exactly. Until some of my distinguished colleagues on the panel can put natural gas more easily into their transportation equipment, natural gas will continue to sell at a discount to oil. Seventy percent of the nation's oil consumption is in transportation.

Mr. LANDRY. And I only have one minute but it is a great point because my question would be if we move natural gas, aka transportation-type fuel, we would recognize there would be a bump in the cost of natural gas. But based upon the supply that we have in the country would that be—how great would that rise be do you believe? Would it be a dollar? Two dollars? Would it be 5–, $6?

Mr. WEINER. I think nobody knows for sure. The outlook for natural gas, especially with shale, is very promising. And so I am afraid that if we do not do as you suggest, the price of natural gas could go way down and that would hurt the natural gas producers and all the associated businesses that supply the natural gas in-

dustry. So I actually think that making natural gas into more of a transportation fuel would help support the domestic industry.

Mr. LANDRY. So it would actually act as a buffer, both protecting the natural gas industry but also keeping the price at a stable level?

Mr. WEINER. That is correct.

Mr. LANDRY. Maybe just a little higher than it is today but nothing near the records that we are seeing oil at?

Mr. WEINER. Nobody knows for sure but I think that is a very good guess, Congressman.

Mr. LANDRY. Thank you so much. Thank you again. Excellent. Sorry, guys.

Chairman TIPTON. Thank you, Mr. Landry and Mr. Weiner. We appreciate that.

I would like to do one follow-up question and I know the ranking member has a couple.

Mr. Ehrlich, I saw your head bobbing when we were talking about being able to use natural gas. Is that a good viable alternative for our agricultural community?

Mr. EHRLICH. Well, I think it could be. Probably the reason my head was bobbing was I was thinking about fertilizer production and the cost of natural gas because that is a huge deal for our producers. And quite frankly, most of the fertilizer coming into the United States today or actually most production of fertilizer in the United States today is imported. And so I was just—I think natural gas would be a good choice for vehicles but I do not know enough about it to make a good comment.

Chairman TIPTON. Thank you. I now yield to the ranking member.

Mr. CRITZ. Thank you, Mr. Chairman. I just have a couple more questions.

Mr. Ehrlich, in your testimony you talked about how you have massive amounts of energy needed to irrigate your crops and that your association is exploring solar power as an alternative. Could you describe what you have been doing in that or what the cooperative has been doing with that and are we at the federal level supporting the efforts in any way?

Mr. EHRLICH. Yes. Well, we are in a coalition with several other members, agricultural-type members like often with the utility companies, trying to develop solar power. More of a community-based economic development program, too, that would allow us to use this solar power to irrigate, to run pumps and motors and things like that. But one of our problems is to use it as economic development we have to have more transmission capacity. And so we have met some opposition with landowners of where the line has to go in order to export power out.

Mr. CRITZ. Right.

Mr. EHRLICH. And so it is a difficult process because there is a very wealthy landowner in that part of the valley and we respect his private property rights, but he has been very successful in using the regulatory process to slow down the project. So I do not know what the outcome will be but that is what we are involved with.

Mr. CRITZ. The landowner is not Ted Turner, is it?

Mr. EHRLICH. No.

Mr. CRITZ. I get the land report every month and I see he is like the largest landowner in the country.

Mr. EHRLICH. He owns land very close to it.

Mr. CRITZ. Okay. See, I was not far off.

Mr. Pingel, the trucking industry is starting to increase its use of alternative fuels such as natural gas, ethanol, and biodiesel. How does that work for the independent trucker? I mean, you are not—you mentioned and I know I have lots of small family trucking firms all around my district and, you know, when you are talking 3, 6, maybe 10 trucks, is it economically feasible for the small transportation company to move from strictly diesel to some sort of either mix or completely natural gas engine?

Mr. PINGEL. Well, some of the states like Minnesota, like I said, being from Wisconsin, they mandated B5, a 5 percent biofuel. And the problem that we ran into at that time was during the winter because biofuel has a tendency to gel up faster. So it is great during the summer. And as far as natural gas, the problem with natural gas is the range on my truck right now in miles per gallon is over 1,000 miles. You cannot carry enough natural gas to go that far, and the range on most of the natural gas trucks that I have seen is right around 300 miles. So you are stopping consistently more times.

Mr. CRITZ. Right. Right. And that is what I have seen as well, is that there is a future but it is not just you flip a switch and you get there.

Well, I appreciate it, Mr. Chairman. Thank you for your testimony. I really appreciate it and this is a great hearing and, you know, from the articles the chairman showed, obviously we are all thinking about gas prices right now. So thank you, Mr. Chairman.

Chairman TIPTON. Thank you, Ranking Member Critz. And I would like to thank all of our witnesses once again for testifying before the Subcommittee today. You highlighted many of the negative impacts of surging gas prices on small businesses in the United States and, more importantly, you have shown us here in Congress that the best way to be able to reduce these heavy burdens is to engage in an "all-of-the-above" approach to high gas prices.

The keystone of this strategy is American oil from American soil. By allowing increased domestic drilling within our borders and within our waters in the near term we can reduce our significant dependence on foreign oil while enabling other more cleaner, more sustainable fuels to be further explored and better integrated into our society, such as natural gas and biofuels.

The recommendations voiced today have not fallen on deaf ears. We will take what we have learned today and inform our colleagues as we move forward or enact or amend policies affecting American small businesses.

I would ask for unanimous consent that members have five legislative days to submit statements and supporting materials for the record. Without objection, so ordered and this hearing is now adjourned. Thank you.

[Whereupon, at 11:05 a.m., the subcommittee was adjourned.]

NACS

Statement of the

National Association of Convenience Stores (NACS)

Submitted for the Record

House Committee on Small Business,
Subcommittee on Agriculture, Energy and Trade

April 14, 2011 Hearing:

"Drilling for a Solution: Finding Ways to Curtail the Crushing Effect of High Gas Prices on Small Business"

The Association for Convenience & Petroleum Retailing

[redacted] • [redacted] • (703) 684-3600 • FAX (703) [redacted] • www.nacsonline.com

On behalf of the member companies of the National Association of Convenience Stores (NACS), thank you for convening this important hearing on the effect of rising gas prices on small businesses. We hope that our comments will help the Committee better understand the overall effects of rising fuel prices not only on those small business that purchase gasoline and diesel fuel, but for those that sell them as well.

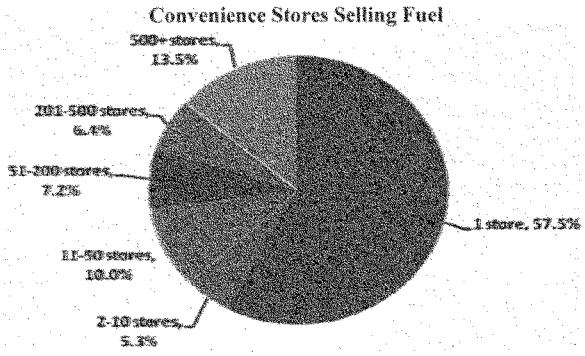
BACKGROUND

NACS is an international trade association comprised of more than 2,200 retail member companies and more than 1,800 supplier companies doing business in nearly 50 countries. As of December 31, 2010, the U.S. convenience and fuel retailing industry operated 146,341 stores of which 117,297 (80.2%) sold motor fuels. In 2009, our industry generated $511 billion in sales (one of every 28 dollars spent in the United States), employed more than 1.5 million workers and sold approximately 80% of the nation's motor fuel.

To best understand how changing fuel prices can affect convenience and fuel retailers, it is important first to understand who owns the stores selling the fuel and how they obtain and resell product.

WHO SELLS AMERICA'S FUEL?

There are 117,297 convenience stores selling fuel in the United States (there are 159,000 total fuel retail outlets). These retailers sell an estimated 80 percent of all the fuel purchased in the country. Overall, nearly 58 percent of the convenience stores selling fuel are single-store operators. These small businesses often don't have the resources to brand their stores as anything beyond the brand of fuel they sell, often leading to consumer misperceptions that they are owned and operated by a major oil company.



In fact, large integrated oil companies, especially since late 2007, have exited the retail business to focus more on resource production and refining operations. ExxonMobil, Shell, BP and ConocoPhillips have either begun or completed the process of selling off all of their directly operated facilities. Of the 117,297 convenience stores selling fuels, about 1,180 – 1 percent – are owned by the one of the five major oil companies.

While the major oil companies are withdrawing from retail, their brands remain. In fact, approximately 50 percent of retail outlets sell fuel under the brand of their refiner-supplier. Virtually all of these branded locations are operated by independent entrepreneurs who have signed a supply contract with a particular refiner/distributor to sell a specific brand of fuel, but these retailers do not share in the profit/loss of their suppliers.

Of the 159,006 fueling stations in the country, approximately 34 percent have a major oil company brand, and another 18 percent carry the brand of a refining company. The remainder – 48 percent – sell a private brand. These outlets are independent business owners who have established their own fuel brand (i.e., QuikTrip, 7-Eleven) and purchase fuels either on the open market or via unbranded contracts with a refiner/distributor.

The remainder of fuels sales in the United States is roughly split equally between traditional service stations without convenience operations and big-box retailers that sell fuels (such as Costco, Walmart and a number of grocery chains).

WHAT INFLUENCES FUEL PRICES

Most people want to know why fuel prices go up and down so frequently. Two key factors that influence retail motor fuels prices include who owns the store and how they get their supplies:

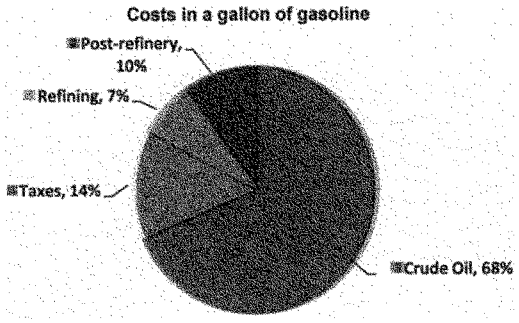
- Branded or unbranded fuels: Typically, stores that sell a branded fuel pay a premium for that fuel, which covers marketing support and signage, as well as the proprietary additive package.
- Dealer tank wagon or rack: Retailers who purchase fuel via dealer tank wagon may pay a higher price than those who get their fuel at "the rack" or terminal. However, rack prices may experience more volatility.
- Length of contract: Even if they sell unbranded fuels, retailers may have a long-term contract with a specific refiner. The length of the contract – which can be 20 years, sometimes longer – can affect the price that retailers pay for fuels.
- Volume: As in virtually every other business, retailers may get a better deal based on the amount of fuel that they purchase, whether based on volume per store or total number of stores.

Even within a specific company, stores may not each have the same arrangements, since companies often sell multiple brands of fuels at different outlets, especially if they have acquired sites with existing supply contracts.

According to the U.S. Energy Information Administration (EIA), there are four factors that make up the price of retail fuels: Crude oil costs, taxes, refining costs and distribution and marketing (which accounts for all costs after the fuel leaves the refinery).

Crude oil prices have, by far, the biggest effect over the retail price of fuels. For one, crude oil costs are responsible for about two-thirds of the cost of a gallon of gasoline. In 2010, crude oil costs were 68 percent of the retail price of gasoline. Second, while there may be slight variations in the costs of refining or distributing and retailing fuels, crude oil prices can experience huge swings. (Taxes are largely static, unless they are based on prices and not set per gallon. Refining

and marketing margins have a much less significant impact on prices, and are often a function of wholesale prices.)



(Source: U.S. Energy Information Administration, cumulative 2010 monthly averages)
(Figures do not add to 100% due to rounding.)

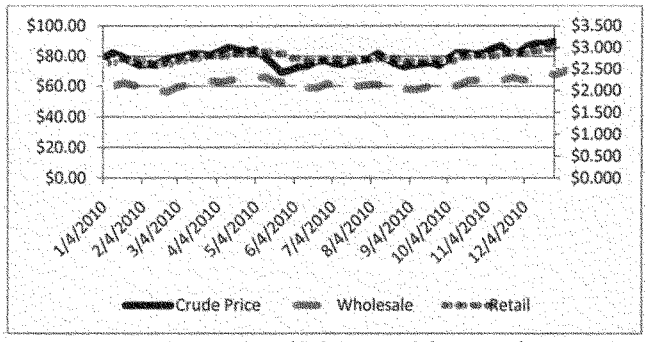
Retail prices are set according to a complex analysis of competitive pressures and the ever-changing wholesale cost of gasoline. Due to differences in supply arrangements, contract terms and delivery schedules, retailers often pay different prices at different times for the gasoline they sell at retail. Retailers must set a price that best balances their need to cover their costs with the need to remain competitive and attract consumers, who are very price sensitive and will shop somewhere else for a difference of a few cents per gallon.

Consequently, retailers often cannot adjust retail prices to fully compensate for changes in their wholesale costs because they must remain competitive with nearby stores who may not have incurred similar changes in costs due to different contract terms, delivery schedules, etc.

When prices go up, retailers may reduce their markup to remain competitive with nearby stores. Likewise, when prices go down, retailers may be able to extend their markup and recover lost profits. In the end, the annual average retail mark-up (the difference between retail price and wholesale cost) has averaged 15 cents per gallon over the past five years.

Crude Oil, Wholesale[1] and Retail Gasoline Prices - 2010

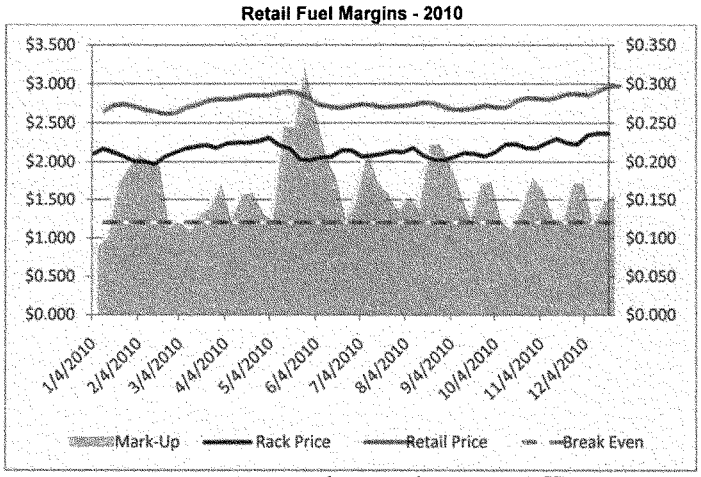
[1] Wholesale prices represented in this and the following charts do not include taxes or freight charges.



(Sources: OPIS "Retail Fuel Watch"; U.S. Energy Information Administration)

The pattern of retail profitability is the opposite of what most consumers think. Due to the volatility in the wholesale price of gasoline and the competitive structure of the market, fuels retailers typically see profitability decrease as prices rise, and increase when prices fall. On average, it costs a retailer about 12 cents to sell a gallon of gasoline. Using the five-year average markup of 15 cents, the typical retailer averages about 3 cents per gallon in profit. In 2010, the average national retail markup was 16.3 cents (5.99%), delivering an average profitability of 4 to 5 cents per gallon.

Over the course of a year, retail profits (or even losses) on fuels can vary wildly. In some cases, a few great weeks can make up for an otherwise dreadful year – or vice versa.



(Sources: U.S. Energy Information Administration, NACS)

With its extreme volatility, fuels retailing is not for the faint of heart – or those with limited access to capital. For example, in 2008 crude oil, wholesale and retail gasoline prices increased dramatically in the first six months – crude oil from a weekly average of $98.17 to a July peak of $142.52; wholesale from $2.514 to $3.501; and retail prices from $3.078 to $4.088.

During this time frame, retailers were put into very precarious financial situations. A typical delivery consists of 9,000 gallons. From the first week in January through the peak in early July, the cost of a delivery jumped from $22,626 to $31,509.

Because retailers were not able to pass through their increased wholesale costs immediately due to competitive pressures mentioned above, many struggled to satisfy their obligations. To continue paying for new deliveries, smaller retailers were forced to extend their lines of credit, which in turn increased their cost of doing business as they worked to service the increased debt. Meanwhile, the retail margin remained relatively static for an average markup of 11.6 cents per gallon (3.44%), just below the average breakeven necessary to sell a gallon of fuel.

Further complicating matters, when retail fuel prices increase consumers often do not have sufficient cash to pay for their purchase. This leads to additional use of credit cards, which already represent approximately two-thirds of the fuel transactions in the nation. This additional use of credit cards coincides with additional fees incurred by the retailer. Since credit card fees are affixed primarily as a percentage of the transaction (approximately averaging 2.5%), per gallon fees in early 2008 increased from 7.7 cents to 10.1 cents, which changes the breakeven calculation for these transactions from an average of 12 cents per gallon to nearly 15 cents. This additional cost further undermined the retailer's ability to cover expenses and retain an operating profit.

At the same time, consumers were feeling the pinch of increased prices. During the first six months of 2008, the nation consumed approximately 69 billion gallons of finished gasoline (about 381 million gallons per day). Every penny change in the retail price represents about $3.8 million per day – money consumers can or cannot spend elsewhere. From the first week in January until the first week in July, consumer spending power declined by $383.8 million per day. This is money that consumers did not have to spend inside the convenience store, where retailers make most of their money[2]. This further diminished the retailer's ability to cover their obligations and in the first half of 2008, many defaulted and were forced out of business.

The rapid decline in crude oil, wholesale and retail prices in the second half of 2008 gave those surviving retailers an opportunity to recover their losses. The weekly average crude price dropped from $142.52 to $32.99, wholesale prices dropped from $3.501 to $1.001 and retail prices dropped from $4.088 to $1.622. Over this time frame, the average retail markup improved to 24.3 cents per gallon, effectively erasing the first six months of losses. But the toll had already been paid by many retailers who were unable to survive until the second half of the year.

CONCLUSION

[2] In 2009, convenience and fuel retailers generated 35.7% of total sales inside the store, but these sales represented 72.7% of pre-tax profit dollars.

The volatility in the retail gasoline and diesel fuel markets is challenging for consumers and retailers alike. In general, fuel retailers can operate more successful businesses when retail prices are lower and consumers have greater spending ability to purchase items inside the store. It is important for policymakers to remember that no two fuel retail outlets are equal – each may operate under different supply contracts, pay different rents for their property, and incur different operating costs. All of these considerations influence their ability to post a competitive price at the pump and still generate a profit.

NACS appreciates this opportunity to share our perspectives on the effect of rising fuel prices on small businesses and we hope we have provided some valuable insight for the committee's consideration.