

**Senate Committee on Foreign Relations**  
**Chairman Richard G. Lugar**  
**Opening Statement for Hearing on**  
**The Hidden Cost of Oil**  
**March 30, 2006**

The Foreign Relations Committee meets today to consider the externality costs of U.S. dependence on fossil fuels. The gasoline price spikes following the Katrina and Rita hurricanes underscored for Americans the tenuousness of short-term energy supplies. Since these events, there is a broader understanding that gasoline and home heating prices are volatile and can rapidly spike to economically damaging levels due to natural disasters, terrorist attacks, or other world events. But, as yet, there is not a full appreciation of the hidden costs of oil dependence to our economy, our national security, our environment, and our broader international goals.

Today, with the help of experts who have thought a great deal about these issues, we will attempt to more clearly define some of these costs. We are cognizant that this is a difficult and imprecise exercise. We are also aware that most, if not all, energy alternatives have some externality costs. But we are starting from the presumption that if we blithely ignore our dependence on foreign oil, we are inviting an economic and national security disaster.

With less than five percent of the world's population, the United States consumes 25 percent of its oil. If oil prices remain around \$60 a barrel through 2006, we will spend approximately \$320 billion on oil imports this year. Most of the world's oil is concentrated in places that are either hostile to American interests or vulnerable to political upheaval and terrorism. More than three-quarters of the world's oil reserves are controlled by national oil companies. And within 25 years, the world will need 50 percent more energy than it does now.

These basic facts demand a major reorientation in U.S. policy aimed at reducing U.S. dependence on fossil fuels. Our goals must be to mitigate the short term costs of our dependence on oil, while pursuing energy alternatives that would reduce the international leverage of petro-superpowers, improve environmental quality, cushion potential oil price shocks, stimulate new high-tech energy industries, and ground the American economy on energy sources that will neither run out nor be cut off by a foreign supplier.

There are at least six basic threats associated with our dependence on fossil fuels. First, oil supplies are vulnerable to natural disasters, wars, and terrorist attacks that can produce price shocks and threats to national economies. This threat results in price instability and forces us to spend billions of dollars defending critical fossil fuel infrastructure and choke points.

Second, over time, finite fossil fuel reserves will be stressed by the rising demand caused by explosive economic growth in China, India, and many other nations. This is creating unprecedented competition for oil and natural gas supplies that drives up prices and widens our trade deficit. Maintaining fossil fuel supplies will require trillions in new investment – much of it in unpredictable countries that are not governed by democracy and market forces.

Third, energy rich nations are using oil and natural gas supplies as a weapon against energy poor nations. This threatens the international economy and increases the risk of regional instability and military conflict.

Fourth, even when energy is not used overtly as a weapon, energy imbalances are allowing oil-rich regimes to avoid democratic reforms and insulate themselves from international pressure and the aspirations of

their own people. In many oil rich nations, oil wealth has done little for the people, while ensuring less reform, less democracy, fewer free market activities, and more enrichment of elites. It also means that the United States and other nations are transferring billions of dollars each year to some of the least accountable regimes in the world. Some of these governments are using this money to invest abroad in terrorism, instability, or demagogic appeals to anti-Western populism.

Fifth, reliance on fossil fuels contributes to environmental problems, including climate change. In the long run, this could bring drought, famine, disease, and mass migration, all of which could lead to conflict and instability.

Sixth, our efforts to facilitate international development are often undercut by the high costs of energy. Developing countries are more dependent on imported oil, their industries are more energy intensive, and they use energy less efficiently. Without a diversification of energy supplies that emphasizes environmentally friendly options that are abundant in most developing countries, the national incomes of energy poor nations will remain depressed, with negative consequences for stability, development, disease eradication, and terrorism.

Each of these threats comes with short and long term costs. As a result, the price of oil dependence for the United States is far greater than the price consumers pay at the pump. Some costs, particularly those affecting the environment and public health, are attributable to oil no matter its source. Others, such as the costs of military resources dedicated to preserving oil supplies, stem from our dependence on oil imports. But each dollar we spend on securing oil fields, borrowing money to pay for oil imports, or cleaning up an oil spill is an opportunity missed to invest in a sustainable energy future.

Certain types of costs are extremely difficult to quantify. We understand that many national security risks are heightened by our oil dependence. But how, for example, would we assign a dollar figure to Iran's use of its energy exports to weaken international resolve to stop its nuclear weapons program?

Yet we should do our best to quantify the externality costs of oil, so we have a clearer sense of the economic and foreign policy trade-offs that our oil dependence imposes on us. As the U.S. government and American businesses consider investments in energy alternatives, we must be able to compare the costs of these investments with the entire cost of oil. Public acknowledgement of the billions of dollars we spend to support what the President has called our "oil addiction," would shed new light on investment choices related to cellulosic ethanol, hybrid cars, alternative diesel, and other forms of energy.

As we address these questions today, we will have the benefit of a distinguished panel of experts. Dr. Hillard Huntington is Executive Director of the Energy Modeling Forum at Stanford University. He is a senior fellow and past president of the United States Association for Energy Economics. He recently coordinated two studies funded by the Department of Energy that evaluated the economic risks of oil price shocks. Mr. Milton Copulos is President of the National Defense Council Foundation. He has advised Secretaries of Defense, Energy, and Interior and was a member of the National Petroleum Council. He is widely published on military affairs and has devoted much study to the military expenditures associated with ensuring the flow of oil. Dr. Gary Yohe is the John E. Andrus Professor of Economics at Wesleyan University. Professor Yohe is widely published on the adaptation and mitigation of climate change. He recently edited *Avoiding Dangerous Climate Change*, the collection of papers on the subject that were prepared for last year's G8 Summit.

We welcome our three witnesses and look forward to their insights.

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