Greater Washington Society of CPAs and GWSCPA Educational Foundation

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January 23, 2008

Wendy W. Payne, Executive Director
Federal Accounting Standards Advisory Board
Mail Stop 6K17V
441 G Street, NW – Suite 6814
Washington, DC 20548

Dear Ms. Payne:

The Greater Washington Society of Certified Public Accountants (GWSCPA) Federal Issues and Standards Committee (FISC) appreciates the opportunity to provide comments on the Federal Accounting Standards Advisory Board's (FASAB) Exposure Draft (ED), *Accounting for Federal Oil and Gas Resources*, dated May 21, 2007.

FISC consists of 19 GWSCPA members who are active in accounting and auditing in the Federal sector. This comment letter represents the consensus comments of our members.

General Comments

The Concept of "Potential Assets" Is Not Fully Developed. While FISC agrees that full and understandable *disclosure* of future potential revenues from royalties on extraction of subsurface and surface resources is desirable, limiting this disclosure to solely oil and gas resources and requiring an asset to be recorded seems inappropriate, especially on the valuation basis provided in the ED.

- **FASAB's Eventual Standard Should Include All Resources** – In addition to oil and gas, subsurface resources include copper, cadmium, nickel, zinc, gold, silver, liquid sulfur, uranium, molybdenum, coal and even water. Surface resources include forestry assets, farming and grazing rights, water and electricity revenues, and even sale of lands. These resources may well equal or exceed any valuation of proved oil and gas resources. Importantly, the ED does not explain why the disclosures and asset recordation is limited solely to oil and gas proved reserves.

- **Record Known "Liabilities" as Well as "Assets"** - If subsurface and/or surface resources potential revenues are recognized as an asset, the costs of realizing such

assets should be accrued as an offsetting liability. In many cases, such costs may be significant. Netting such potential revenue is consistent with some of the projection methods for future liabilities of social benefits, e.g., the estimated payments thereunder are netted against the estimated employee withholdings and premium receipts therefor.

- **Disclose vs. Valuation** – The ED comprises 83 pages for oil and gas resources alone. Covering all possible items that could be converted into cash at some date would constitute likely the most complex accounting standard ever issued. FISC recommends that the eventual Standard be broken into parts with an initial Standard focusing on *disclosure* of potential resources, and proceed with a subsequent Standard on *valuation* (if this is the eventual FASAB decision). FISC does not concur that potential oil and gas royalties is an asset that should be recorded at this time.

- **Avoid a "Cookbook" Type of Standard** – The specificity of determining the various classes and subclasses of potential oil and gas resources and sources of information thereon will likely require numerous additional Standards as the sources of information change, new and better sources are identified, or current sources are discontinued. If FASAB goes forward with the Standard, the "how to do it" section should be considerably shortened to permit flexibility of the Federal agency responsible for administering subsurface and surface resources to select the best available source of data upon which to make estimates of recoverable resources and valuation thereof. FISC also recommends that actual journal entries are unnecessary if properly described in the eventual Standard; a FASAB Implementation Guide or Treasury/OMB directive should address journal entries to insure that entries meet Treasury's SGL requirements.

"Potential Assets" From Oil and Gas Resources Not Distinguished From Other "Potential Assets." The Federal government has significant unrecorded assets. For example, gold is recorded at $42.22/fine troy ounce, while the market value was $743.00/fine troy ounce, at September 30, 2007 (see page 55 of the 2007 *Annual Financial Report*.) Certainly, the largest potential revenue source of the Federal government is its ability to enact and collect the individual income tax (state and local governments previously used to report such an asset in the caption "Amount to be Provided" – This concept has been abandoned under recent GASB standards). Both gold holdings and future income tax revenues are far easier to quantify and value than potential oil and gas royalty income. The ED does not clarify why oil and gas resources have been singled out for valuation and asset recognition, or whether the ED is the first of numerous future Standards for other resources. If so, serious comparison issues will arise as "new potential assets" are recorded pursuant to future additional Standards.

The Eventual Standard Would Present Significant "Lack of Symmetry" in Society. The ED properly proposes that a liability for the Federal government's agreements to share potential royalty assets with state governments, generally about 50% for most states and 90% for Alaska. However, it is unlikely that any state government preparer of financial statements or independent auditors thereof would concur that the "assets" at the state level should be recorded. Attachment A hereto includes the list of recipients of all mineral royalties shared with states, and these amounts are significant for the principal recipients. The "liability" payable to states can change; for example during the past fiscal year 2007 alone, the royalties provided to states changed in two ways – first, for states along the coastline, royalty sharing was increased for offshore royalties and second, the "pool" of royalties available for distribution to states changed to net the pool for MMS' costs, legislatively established at 4% (incidentally, this provision was in the Omnibus Budget Bill signed on December 26, 2007, after the end of the closing of the books on November 15, 2007) reducing the net royalties to the Federal government and states by 2% each.

Major Fluctuations Will Occur in the Ultimate Amounts Recorded as Assets and Offsetting Payments to States. Knowledgeable industry observers have very mixed views on the short- and long-term production of oil and gas, likely prevailing prices thereof, and even the continued use thereof in the world economy. An article in the January 2008 issue of *Conde Nast Portfolio* magazine in Attachment B hereto is just one such prediction that the current $100/barrel of crude will not continue indefinitely due to improved technology in recovering resources already discovered or even "capped out," new discoveries, changes in usage of petroleum, alternate energy sources, the overhang of the shale oil and tar sands with oil prices in excess of recovery costs, etc. Others predict that, in the short-term, oil prices could increase to $200/barrel. Since future economic extraction of any subsurface resource depends on a plethora of uncertainties over long periods of times, FISC questions whether it is wise to record assets subject to such fluctuations over which the Federal government has no control. FISC contrasts this with the relatively known metrics for estimating liabilities for social programs since population, age, gender and other factors are reasonably well estimable.

There are also situations that, regardless of potential recoverable or realizable resources that may exist, public policy will prevent such recovery, including resources currently recoverable or realizable, but will be prohibited by future legislation. Our National Parks, Fish and Wildlife Refuges, including the Alaska National Wildlife Refuge (ANWR) are good examples of this. This clouds the distinction between proved reserves and all other potential resources.

Specific Comments

If some form of the ED advances to a Standard, FISC has a number of comments.

- **Throughout Text** – The ED uses the plural form "standards" while the eventual Standard will be singular.

- **Valuation** – Paras. 5 through 15 specify how the "current regional average prices" are to be established and Para. 15 values the proved reserves at that price. This effectively will result in an adjustment of the "asset" even if no oil or gas is extracted during the year because these resources are subject to world prevailing prices. In a falling market, this overstates the "asset" and in a rising market, this understates the "asset." FISC favors a "fair value" approach to minimize such fluctuation as explained in the Alternate View beginning in Para. A119.

- **Valuation** – FISC questions why, if discounted valuations are to be used in the many types of liabilities recorded (pensions, Social Security, post-employment health/life insurance benefits, etc.), discounted values would not be used for oil and gas "assets."

- **Statement of Net Cost/Para. 28** – Since oil and gas royalty "assets" are a "sovereign asset", FISC does not understand why gains or losses are a part of Net Cost since neither the gain or loss has been realized. This will cause fluctuations that could exceed the otherwise "bottom line" of net operating costs in excess of revenues (i.e., annual operating deficit). What Administration, for example, would want a loss in value of future royalties wiping out an entire surplus?

- **Effective Date of Eventual Standard/Para. 48** – The "periods ending after September 30, 2009," which is FY 2010, should be changed to move the date forward several years to permit Federal government agencies, principally Interior, to develop systems to estimate quantities of proved reserves and all other reserves, and value proved reserves.

- **Basis for Conclusions -** The ED cites numerous sources of data, e.g., Cambridge Energy Research Associates, and Department of Energy's Energy Information Administration – numerous laws, years of events, etc., all of which are well known "data literate" users of these statistics. FISC believes that changes are most likely to occur for this information, which immediately may render the eventual Standard obsolete or require it to be amended. FISC believes that this ED area in particular is in need of revision to minimize premature life of the Standard.

- **ED Appendix C** – FISC suggests that this guidance be incorporated in an Implementation Guide or some other FASAB, Treasury or OMB document. See "cookbook" comment above.

Responses to Questions

Q1 – "The proposed standards would provide for recognition of the Federal government's royalty share of proved oil…"

FISC believes that it is premature to capitalize any value for proved reserves under either method. FASAB has not explained why capitalization is restricted solely for proved oil and gas resources, why only subsurface minerals are solely considered (vs. surface resources), and why the capitalization concept is not extended to other assets, e.g., gold holdings and future income tax revenues. In short, FISC believes that FASAB is incurring a risk of discrediting the entire financial reporting standards that it has worked diligently and successfully to establish by literally "counting the chickens before they are hatched."

Q2 – "The Board proposes to value the Federal government's royalty share of proved reserves based on average regional prices…"

FASAB should seriously consider the evolving world financial reporting movement to fair value accounting – See Alternate View – and value any proved resources at prevailing market prices as of fiscal year end on September 30. Also, considering the use in other FASAB Standards of discounting valuations for future events, FASAB should consider standardizing its valuation methods.

Q3 – "Some Board members believe that the amount of information proposed to be disclosed …is excessive…"

FISC agrees that simplification is necessary. Since the users of reserve data are well aware of the data sources cited in the ED and their limitations, these "reserve-literate" experts already have all the data they need.

FISC does favor some additional disclosure of all subsurface and surface resources in RSI or elsewhere in the financial statements of the overall Federal Government.

Q4 – "The proposed standards would require that an estimated value for royalty relief be reported as RSI…"

This disclosure appears to be a reaction to the publicity raised by royalty relief in general or errors in the granting thereof. This is another source of "tax expenditures" or "foregone revenue." FISC concurs that all such foregone revenues be disclosed as was the practice in the early years of the prototype consolidated financial statements. Many readers of financial statements will be as interested in foregone revenues due to other types of relief as they would be in royalty relief.

Pages 285 through 313 of the FY 2008 President's Budget Submission contain "tax expenditures" estimates for tax provisions effective as of December 31, 2006. This 28-page tome should be condensed into a table, to which royalty relief, together with forms of subsidy other than tax provisions, should be added.

Q5 – "…SFFAS 7…requires that agencies report on assets held in a fiduciary capacity…Interior manages oil and gas resources …"

The Uniform Principal and Income Act, enacted by at least 43 states limits responsibility of a fiduciary to cash received, invested and disbursed, and prudent holding of non-cash assets. While SFFAS 31 will require disclosure of land assets held in the two Indian Trust Funds, it will be extraordinarily difficult to record proved oil and gas resources in the financial statements of the two Indian Trust Funds, and certainly a challenge for a November 15 completion of the audits thereof. The number of oil and gas leases on Indian lands (approximately 55 million acres – 45 million tribally-owned and 11 million owned by individual Indians) is disproportionately large since the individual holdings are small compared to other Federal Government leases on its own holdings.

FISC concurs that extension of reporting of oil and gas leases and valuing the proved reserves related thereto would cost far more than any useful information provided therewith. Interior now reports undivided and divided land interests owned by tribes and individual Indians and leases thereon (exploratory, producing and non-producing) in quarterly statements to the tribal and individual account holders. This can be seen in the following data taken from the Mineral Management Service web site. (This information has either been taken directly from the web site or has been derived from information taken from the website.)

MMS Summary of Oil and Gas Lease Data
Producing and Non-Producing Leases – Fiscal Year 2007

	American Indian Leases	Total Federal Government Leases
Number of Leases	4,119*	63,610
Percentage of Total Leases	6.1%	93.9%
Leased Acreage	2,069,459**	91,595,981**
Percentage of Leased Acreage	2.2%	97.8%
Average Acreage Per Lease	502	1,440
Total Oil & Gas Royalties	$317,735,000	$9,256,032,000
Percentage of O & G Royalties	3.3%	96.7%

*Many of these leases cover lands jointly owned by one or more tribes and many undivided individual Indian interests.

**67,792,121 (74.0%) Federal Government acres are non-producing vs. 152,971 (7.4%) non-producing Indian acres.

Q6 - "The proposed standards would require the component entity to provide extensive disclosures and RSI…"

FISC recommends a reversal of the degree of proposed disclosures. Since subsurface and surface potential revenue sources are sovereign assets, the major disclosures more properly should be included in the overall U.S. Government *Consolidated Report*. The particular agency administering a revenue source, which relates to the sovereign, is not particularly significant, especially since the administrator can be changed in agency reorganizations, e.g., the recent establishment of the Department of Homeland Security.

Q7 –"The proposal includes accommodations intended to reduce the cost and burden of implementation…"

a. Proved reserves may well be economically non-recoverable due to recovery costs, existing or future environmental laws or regulations, changed technology, changes in prevailing world market prices, etc. FISC believes that the eventual Standard must provide guidance for such limitations on proved reserves,

particularly if other subsurface or surface revenue sources eventually come under a capitalization provision.

b. FISC recommends fair value.

c. FISC believes that value is determined by what a seller accepts and a buyer is willing to pay as of the end of the fiscal year.

d. We are a nation of laws, and statutory or contractual rates must prevail over market rates where statutory or contractual rates apply. Differences may be equivalent to "revenue forgone" or contracting errors in the case of lower rates than market, and favorable rates in cases of market rates below statutory or contractual rates.

e. Fair value would consider regional variations.

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This comment letter was reviewed by the members of FISC, and represents the consensus views of our members.

Very truly yours,

Daniel L. Kovlak
FISC Chair

Attachment A: http://www.mms.gov/ooc/press/2007/press1204.htm

Attachment B: http://www.portfolio.com/views/columns/economics/2007/12/17/Why-Oil-Prices-Will-Drop

The NewsRoom

Release: # 3759
Date: December 4, 2007

Thirty-four States Earn $1.9 Billion in Royalty Receipts

MMS Reports FY 2007 Disbursements

DENVER – Thirty-four states earned more than $1.9 billion during Fiscal Year 2007 as part of their share of federal revenues collected by the Department of the Interior's Minerals Management Service (MMS).

"These revenues from mineral production on federal lands play a crucial role in many state budgets," said Randall Luthi, MMS director. "The funds support everything from education to infrastructure improvements and capital projects."

MMS is the federal bureau within the Department of the Interior responsible for collecting, auditing and disbursing revenues associated with mineral leases on federal and American Indian lands. Disbursements are made to states on a monthly basis from royalties, rents, bonuses and other revenues collected by MMS.

The $1,972,322,944 distributed to states during the Fiscal Year that ended Sept. 30, 2007 compares with Fiscal Year 2006 payments to states that totaled more than $2.2 billion. A preliminary analysis indicates the slight decline is the result of several factors, including lower natural gas prices during the fiscal year and a drop in lease sale bonuses from the previous year, among others.

Fiscal Year 2007 marked the first full year that MMS distributed funds from geothermal energy production directly to the individual counties where that production occurs. Luthi noted that the Energy Policy Act of 2005 mandated that 25 percent of receipts from geothermal energy production be disbursed directly to counties where that production occurs, in an effort to increase use of that alternative energy resource. As part of that mandate, and included in the $1.9 billion distributed overall, MMS distributed more than $4.3 million to 32 counties in the states of California, Idaho, New Mexico, Nevada, Oregon and Utah.

During Fiscal Year 2007, the state of Wyoming led all states by receiving more than $925 million as its share of revenues collected from mineral production on federal lands within its borders, including oil, gas and coal production. New Mexico's share was nearly $553 million, while the state of Utah received more than $135 million. Other energy-producing states sharing revenues included Colorado with more than $122 million; California with more than $61 million; Montana with $39.1 million; Louisiana at $24 million; Alaska at $21.7 million; and Texas, which received approximately $21.6 million in Fiscal Year 2007.

The disbursements represent the states' cumulative share of revenues collected from mineral production on federal lands located within their borders, and from federal offshore oil and gas tracts adjacent to their shores. For the majority of onshore federal lands, states receive 50 percent of the revenues while the other 50 percent goes to various funds of the U.S. Treasury, including the Reclamation Fund for water projects. Alaska receives a 90 percent share as prescribed by the Alaska Statehood Act. States may also receive matching appropriations from the offshore oil and gas royalty-funded Land and Water Conservation Fund, the Reclamation Fund, and other special-use funds.

In addition, Texas, Alabama, Louisiana and Mississippi with producing federal offshore tracts adjacent to state waters receive 27 percent of those mineral royalties. Remaining offshore revenues collected by the MMS are deposited in various accounts of the U.S. Treasury, with the majority of those revenues going to the General Fund.

States receiving revenues through Fiscal Year 2007 include:

Alabama	$14,173,908.88
Alaska	$21,796,671.52
Arizona	$41,792.37
Arkansas	$8,143,230.86
California	$61,240,940.54
Colorado	$122,894,226.71
Florida	$6,649.38
Idaho	$4,729,812.55
Illinois	$205,558.80
Indiana	$8,046.75
Kansas	$1,876,305
Kentucky	$714,750.97
Louisiana	$24,029,594.03

Michigan	$616,971.05
Minnesota	$13,126.30
Mississippi	$2,226,547.50
Missouri	$3,598,352.32
Montana	$39,158,279.03
Nebraska	$24,176.98
Nevada	$7,663,678.82
New Mexico	$552,934,465.33
North Dakota	$13,775,447.53
Ohio	$493,091.99
Oklahoma	$6,988,592.26
Oregon	$558,122.83
Pennsylvania	$55,584.87
South Carolina	$277.50
South Dakota	$1,007,068.91
Texas	$21,667,264.63
Utah	$135,429,658.25
Virginia	$233,474.14
Washington	$366,365.07
West Virginia	$389,004.34
Wyoming	$925,261,906.81
Total:	$1,972,322,944.82

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MMS: Securing Ocean Energy & Economic Value for America
U.S. Department of the Interior

#8	Dan Kovlak	Non-Federal - Other

ECONOMICS

by John Cassidy

The Coming Oil Crash

Dec 17 2007

Crude at $100 a barrel makes good headlines but ignores basic economics. Why oil prices are in for a 50 percent drop.

Crude Awakening

For now, oil prices are near record levels. But anyone who believes high prices will last forever ignores these trends, which will, sooner or later, make a slump inevitable.

Photoillustration by: Reena De La Rosa

If you haven't got the message that something disturbing is happening in the oil world, stop by my office. On my desk, I have a pile of books a foot high with titles like *Out of Gas, The End of Oil,* and *Twilight in the Desert.* The authors range from geologists to journalists to policy wonks, and they all tell the same story.

For years, oil industry executives dismissed fears of an energy crisis, attributing rising gasoline prices to unrest in the Middle East, Wall Street speculation, and temporary interruptions in supply. But recently, as the price of crude has bounced around $100 a barrel, even some establishment figures have been making alarmist noises. The Paris-based International Energy Agency warned of a possible "supply crunch" within five years. Its chief economist, Fatih Birol, said prices could reach such a high level that "the wheels may fall off" the global economy. In the U.S., the National Petroleum Council, a federal advisory group,

said that as the economies of China and India continue to expand, global energy consumption will rise by 50 percent over the coming quarter of a century. "There is no quick fix," said Lee Raymond, former chairman of Exxon Mobil, who leads the council.

Perhaps not. But the experts who are predicting the worst, based on geology and geopolitics, are missing the crucial role that economic incentives play in determining the price of crude. The tripling of oil prices since the summer of 2003 has unleashed forces that within the next two or three years will bring oil prices tumbling back down to below $50 a barrel. Looking even further ahead, prices could easily fall to $30 a barrel or even lower. So before you trade in your Cadillac Escalade for a Toyota Prius, think twice: $1.50-a-gallon gas might not be gone forever.

The key to understanding where prices are headed is distinguishing between the short run and the long run. In a time frame of anything shorter than five years, the supply of crude is more or less fixed. Drilling for oil is an arduous and unpredictable process. Even after a new hydrocarbon reservoir is discovered, ramping up output takes years. Current production capacities reflect investment decisions made in the late 1990s or earlier.

Today, OPEC has the ability to produce about 35 million barrels of crude a day; the rest of the world can produce perhaps 50 million barrels a day. As recently as 2003, this seemed like plenty. Since then, though, global demand has grown rapidly, and a series of catastrophes—some natural (hurricanes Rita and Katrina), some man-made (war in Iraq and unrest in Nigeria and Venezuela)—have curtailed production, causing supply to dip below demand. In September, the global demand for crude reached 85.9 million barrels a day, whereas global supply was just 85.1 million barrels a day, according to I.E.A. figures.

When shortages emerge in any market, prices spike. If the imbalance is expected to continue, speculators move in and drive prices even higher. Oil is no exception. In the fall, as crude inventories declined and the rhetorical battle between the U.S. and Iran escalated, trading volume shot up.

With prices close to the inflation-adjusted record, energy companies and governments are investing heavily in facilities that generate crude and crude substitutes. Consumers of fuel oil and gasoline are starting to economize, and over time, these changes in behavior will shift the balance of power in their favor. When that happens, an oil glut will emerge, and the price will plummet.

Already, in Texas and California, hundreds of mothballed, low-producing stripper wells have been brought back into production. In Africa, the Chinese government is making development deals with Sudan, Chad, the Congo Republic, and other impoverished nations with unexploited reserves. In the Canadian province of Alberta, Shell and other energy companies are building massive strip mines to access local tar sands, which can be converted into synthetic oil or refined directly into petroleum at a cost of roughly $30 a barrel. Some experts believe the sands contain more oil than the subdeserts of Saudi Arabia.

Not very long ago, energy companies were slashing their exploration and drilling budgets, refusing to finance any project unless it could generate crude for $15 or $20 a barrel. But since 2003, when the price of crude rose above $30 a barrel, the industry has relaxed its financial assumptions and beefed up capital spending. In the past four years, Exxon Mobil, the world's largest oil company, has invested more than $60 billion in exploration and development. Between now and 2010, the company plans to begin pumping oil or gas from no fewer than 20 new projects.

Besides Canada, the oil majors are also returning to areas that weren't economically viable when oil was cheap, including the Arctic Ocean and the deep waters of the Gulf of Mexico. The industry's efforts aren't confined to searching for new reserves. It is also investing heavily in high-tech imaging machines and steerable drills that raise yields from existing reservoirs, where historically only the most readily available crude, typically 30 to 40 percent of the total, was recovered. (Extracting the rest was considered too costly, so it was left alone.)

When experts claim that oil is running out, what they really mean is that cheap oil is running out. About this, they may be right. Outside of Saudi Arabia, Iraq, and a few other countries, it is no longer possible to recover large quantities of crude

for a dollar or two a barrel. But there are plenty of places where oil can be produced for $20 or $30 a barrel, let alone the $100 range where it has been trading recently.

And the list of potential substitutes for crude is long. Natural gas can be converted to a liquid fuel that produces few pollutants. Venezuela has big reserves of tar sands, as does Utah. Neighboring Colorado has oil trapped in shale, which industry engineers are trying to extract by slowly heating the rock under the Green River Basin. Corn, sugar, and potatoes can be distilled into ethanol, a perfectly good transport fuel, as can wood chips, straw, and other biomass. And as demand for ethanol has surged in recent years, farmers throughout the Midwest have taken advantage of generous federal subsidies to convert their fields to corn, the price of which doubled in the past 18 months. (When oil prices fall, such crop switching may prove to be a costly mistake.)

With energy supplies expanding and the demand for oil showing signs of faltering, it won't be very long before economic fundamentals reassert themselves. If oil were a normal commodity, competition would eventually drive the price down to a level close to the current cost of production, which at the margin is probably somewhere between $20 and $30 a barrel.

Of course, the oil market is hardly a textbook case of open competition: The OPEC cartel controls 40 percent of the supply, and geopolitics is an ever-present factor, as is speculation. The recent surge toward $100 a barrel was a dramatic demonstration of how traders can cause prices to become unmoored from costs for a lengthy period. But that also means that once market sentiment turns, the fall in prices could be just as dramatic.

Nobody in the oil market—not Wall Street, not Exxon Mobil, not even OPEC—can sustain prohibitively high prices for very long, a point that Sheik Yamani, the Saudi oil minister during the oil price shocks of the '70s and '80s, recognized. "If we force Western governments to invest heavily in finding alternative sources of energy, they will," he said in 1981, shortly after OPEC production cuts caused the price of crude to hit a record of $39.50 a barrel—roughly $100 a barrel in 2007 dollars. "This will take them no more than seven to 10 years and will result in their reduced dependence on oil as a source of energy to a point which will

jeopardize Saudi Arabia's interests."

Most people ignored Yamani's warning, but he was right. Between 1979 and 1983, oil consumption in the non-Communist world fell by 6 billion barrels a day, or more than 10 percent. Motorists bought smaller cars. Homeowners threw out their oil furnaces. Power stations switched to coal, nuclear fuel, and natural gas. And this all happened at a time when new oil fields in Alaska, Mexico, and the North Sea were coming onstream in a big way. The result was an excess supply of crude and a huge drop in prices. In 1986, the cost of a barrel of crude fell to as low as $11.

The oil industry entered a prolonged slump, devastating Texas and other producing areas. For most of the '90s, the cost of a barrel of crude stayed below $20. At the end of 1988 and the start of 1989, it fell below $10, and you could get change out of a dollar for a gallon of gas.

I'm not saying that the oil price will slink all the way back to $10 a barrel. But a reckoning is inevitable. Serious divisions are emerging within OPEC about 2008 production levels. Presidential candidates in the U.S. are calling for tougher fuel-economy standards. Many Western countries, the U.S. and Britain included, have been making plans for a new generation of nuclear power plants. In the oil market, the laws of supply and demand sometimes appear to have been suspended. Ultimately, however, they do work.