PIRINC

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LOOK BEFORE YOU LEAP

Don't Cut the Gasoline Tax

PIRINC has received a number of requests for comment regarding proposals to reduce gasoline taxes and or "freeze" margins to provide some "relief" for consumers facing today's extreme high prices. While well intentioned, it's simply a bad idea.

Prices have reached these levels because high demand, encouraged by strong growth in incomes, have pushed very close to the industry's near-term ability to supply. This is the case for world crude oil markets where there is very little overall spare capacity, and virtually none for the types of crudes (light), low sulfur) most easily processed into gasoline. This is also the case for refining capacity, where years of poor returns, and particularly in the U.S., expensive regulatory requirements have discouraged investment in new capacity. Higher prices create incentives for corrective action to reduce demand and expand supply — and, thereby, moderate the initial surge in prices. But the scope for such actions in the near term is very limited. As a result, prices tend to rise quickly and disproportionately in response to short-term tightening of already strained markets.

In such circumstances, a reduction in what by world standards is an exceptionally low tax to begin with is counter-productive. It would tend to prop up demand in a tight market, putting additional pressure on immediate crude and pre-tax gasoline prices. While all consumers are having to pay more at the pump these days, not all are experiencing outright hardship as a result. High energy prices are regressive. They tend to hurt disproportionately low-income wage earners and those on fixed incomes. Thus, the proposed policies are too heavy handed "helping" those who don't need it as well as those who do. What is needed in the short run is a targeted and not a shotgun approach.

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A measure that gives the greatest financial benefits to those driving the largest, heaviest, and lowest MPG vehicles the longest distances with no distinction as to ability to pay seems particularly inappropriate. Such a measure seems a wasteful use of government resources, particularly at a time of high deficits.

There are precedents for targeted relief from high-energy costs for low-income consumers. The LIHEAP program assists low-income families facing high-winter heating bills so some form of relief for low-income drivers could be considered. Some form of relief could help low-income wage earners stay on the payroll and not the welfare role. Since most people must drive to work, an adjustment to the Earned-Income Tax Credit could be considered as a potential rough-and ready way of providing targeted relief. Gasoline price increases have garnered most of the media attention, yet households will face a larger increase in heating bills this winter. The average gasoline consumer is facing an annual increase of $200-300 but his oil or natural gas heating bill for just the coming winter is likely to rise by nearly twice that level.

In a market economy price sends a message. We need to pay more attention to what this message is saying rather than promote creative yet non-productive ideas that mute the price signal.

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