

Raise the Gas Tax

By N. Gregory Mankiw

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With the midterm election around the corner, here's a wacky idea you won't often hear from our elected leaders: We should raise the tax on gasoline. Not quickly, but substantially. I would like to see Congress increase the gas tax by \$1 per gallon, phased in gradually by 10 cents per year over the next decade. Campaign consultants aren't fond of this kind of proposal, but policy wonks keep pushing for it. Here's why:

The environment. The burning of gasoline emits several pollutants. These include carbon dioxide, a cause of global warming. Higher gasoline taxes, perhaps as part of a broader carbon tax, would be the most direct and least invasive policy to address environmental concerns.

Road congestion. Every time I am stuck in traffic, I wish my fellow motorists would drive less, perhaps by living closer to where they work or by taking public transport. A higher gas tax would give all of us the incentive to do just that, reducing congestion on streets and highways.

Regulatory relief. Congress has tried to reduce energy dependence with corporate average fuel economy standards. These CAFE rules are heavy-handed government regulations replete with unintended consequences: They are partly responsible for the growth of SUVs, because light trucks have laxer standards than cars. In addition, by making the car fleet more fuel-efficient, the regulations encourage people to drive more, offsetting some of the conservation benefits and exacerbating road congestion. A higher gas tax would accomplish everything CAFE standards do, but without the adverse side effects.

The budget. Everyone who has studied the numbers knows that the federal budget is on an unsustainable path. When baby-boomers retire and become eligible for Social Security and Medicare, either benefits for the elderly will have to be cut or taxes raised. The most likely political compromise will include some of each. A \$1 per gallon hike in gas tax would bring in \$100 billion a year in government revenue and make a dent in the looming fiscal gap.

Tax incidence. A basic principle of tax analysis -- taught in most freshman economics courses -- is that the burden of a tax is shared by consumer and producer. In this case, as a higher gas tax discouraged oil consumption, the price of oil would fall in world markets. As a result, the price of gas to consumers would rise by less than the increase in the tax. Some of the tax would in effect be paid by Saudi Arabia and Venezuela.

Economic growth. Public finance experts have long preached that consumption taxes are better than income taxes for long-run economic growth, because income taxes discourage saving and investment. Gas is a component of consumption. An increased reliance on gas taxes over income taxes would make the tax code more favorable to growth. It would also encourage firms to devote more R&D spending to the search for gasoline substitutes.

National security. Alan Greenspan called for higher gas taxes recently. "It's a national security issue," he said. It is hard to judge how much high oil consumption drives U.S. involvement in Middle Eastern politics. But Mr. Greenspan may well be right that the gas tax is an economic policy with positive spillovers to foreign affairs.

Is it conceivable that the policy wonks will ever win the battle with the campaign consultants? I think it is. Even after a \$1 hike, the U.S. gas tax would still be less than half the level in, say, Great Britain, which last I checked is still a democracy. But don't expect those vying for office to come around until the American people recognize that while higher gas taxes are unattractive, the alternatives are even worse.

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