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Paying More at the Pump: Energy Bill Would Increase Gas Prices

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Congress is currently debating energy policy legislation that could result in significantly higher prices for gasoline consumers. A review of H.R. 6, including the just-completed section on tax changes, reveals that the bill could increase the price of regular unleaded gasoline from \$3.06 per gallon (the early December national average) to \$5.02 in 2016.

The bill aims to slow and ultimately reverse the growth of carbon emissions from many sources, among them gasoline-powered vehicles. It does so mainly through provisions requiring higher Corporate Average Fuel Economy (CAFE) standards for cars and more biofuel content in retail gasoline. All of the federal government spending associated with the bill's mandates and programs is paid for through a series of tax increases, most of which fall on the producers of gasoline. The combined effects of these policy changes will cause retail gasoline prices to increase.

Biofuel Content. The requirement to increase the biofuel content of retail gasoline reduces flexibility in the nation's gasoline supply and adds to the production costs—the latter stemming primarily from the higher costs of producing ethanol and cellulosic alcohol.¹ Taken together, these two factors will affect gas prices in the short term as the structure of gasoline production changes to conform to the bill's requirements.

Increasing CAFE Standards. If the nation's automobile and truck fleet achieves the higher fuel efficiency targets, demand for gasoline will fall,

exerting a downward pressure on gas prices. However, that pressure offsets only about a fourth of the increased costs resulting from biofuel requirements. Some analysts might argue that the downward pressure will be greater; however, recent history has demonstrated that higher fuel efficiency standards have a modest effect on price.

Price Controls. The least environmentally focused initiative associated with this energy legislation is the one most likely to increase prices. Earlier this year, the House adopted—and the Senate seriously considered—stand-alone legislation to prevent “price gouging,” or especially high prices that a government agency would find well in excess of “market prices.” Many times over the past 100 years, well-meaning efforts to cap prices in order to protect U.S. consumers resulted in unintended reductions in supply and higher prices. A simple economic truth is that high prices spur producers to increase supply, which ultimately lowers prices for consumers. When policymakers set price caps to combat “price gouging,” the result is the opposite of the one intended. Consumers increase their demand as a result of the capped price, but producers do not face any incentive to meet that demand.

This paper, in its entirety, can be found at:
www.heritage.org/Research/EnergyandEnvironment/wm1729.cfm

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	2008	2010	2012	2014	2016
Regular Unleaded Price Trend without Policy Changes	\$3.06	\$3.33	\$3.63	\$3.94	\$4.30
Price Effect of Biofuel and Threatened Price Caps	0.18	0.27	0.38	0.50	0.64
Price Effect of Tax Law Changes	0.03	0.06	0.06	0.07	0.08
New Price with Policy Changes	3.28	3.66	4.07	4.52	5.02
Effect of Policy Changes on Price	0.22	0.33	0.44	0.57	0.72

Source: Center for Data Analysis calculations.

Supply fails to keep pace with demand, resulting in rationing or supply “brown outs.”

Increased Taxes. The bill contains a number of tax law changes that will also affect gasoline prices. Among the most prominent are the following:

- Increased taxation of income derived from foreign oil and gas production;
- Reduction in the deduction taken by oil companies for domestically produced oil and natural gas production; and
- Change in the amortization period for oil and gas exploration equipment, which raises oil company tax payments.

The loss of current gasoline company tax credits is particularly dangerous to consumers, since it is a large loss (about \$13 billion over 10 years).² Tax-

paying corporations tend to recoup increased tax payments in the form of higher retail prices.

Taken together, the four factors will raise the price of gasoline by the estimated amounts shown in Table 1.

The national average per-gallon price of gasoline in early December 2007 was \$3.06.³ This average is the basis for the national and state-by-state increases in the per-gallon cost of regular unleaded gasoline prices over the next several years. Heritage analysts projected estimates of gasoline prices through 2016 by first adjusting the December 2007 rate for inflation⁴ and then adding the calculated change in gas prices⁵ as a result of the provisions in H.R. 6 to each state’s average cost. Gas consumers can expect to pay between \$3.07 and \$3.66 per gallon for gas in 2008 after adding in the estimated

1. For more on the costs of ethanol and cellulosic alcohol production, see Ben Lieberman, “The Compromise Energy Bill: Harmful Regulation, Not Affordable Energy,” Heritage Foundation *WebMemo* No. 1721, December 5, 2007, at www.heritage.org/Research/EnergyandEnvironment/wm1721.cfm.
2. Several other revenue-raising provisions in the legislation do not relate to oil companies or affect gasoline prices. When these other tax increases are included, the total amount raised over 10 years is \$19.7 billion.
3. Data on average per-gallon cost of gas was collected on December 7 from www.fuelgaugereport.com/sbsavg.asp by selecting each state and recording the value in the “Current Avg.” field.
4. Average prices for December 2007 were carried over to 2008 and were not adjusted for inflation. Gas prices in 2010, 2012, 2014, and 2016 were adjusted for 8.8 percent inflation (4.4 percent inflation over 2 years = 8.8 percent inflation adjustment). This rate was calculated based on the U.S. average weekly price for unleaded from August 1990 through December 2007. Weekly Retail Gasoline and Diesel Prices are available from the Energy Information Administration at http://tonto.eia.doe.gov/dnav/pet/pet_pri_gnd_dcus_nus_w.htm.
5. This is the estimated impact that the energy bill would have on regular unleaded gasoline prices, as shown in Table 1.

Estimated Impact of H.R. 6 on States' Average Regular Unleaded Gasoline Prices

State	Average Price Per Gallon, December 2007	Estimated Average Price Per Gallon in 2008	Estimated Average Price Per Gallon in 2016	Additional Annual Cost of Gas Per Person in 2016 (Relative to 2008 Prices)*
Alabama	\$2.97	\$3.19	\$4.89	\$900.41
Alaska	3.21	3.43	5.23	829.88
Arizona	3.01	3.23	4.95	655.69
Arkansas	2.96	3.18	4.88	868.96
California	3.39	3.61	5.47	773.89
Colorado	3.01	3.22	4.94	746.66
Connecticut	3.25	3.46	5.27	788.76
Delaware	2.98	3.20	4.91	923.34
District of Columbia	3.11	3.33	5.08	378.06
Florida	3.13	3.34	5.11	873.96
Georgia	3.00	3.22	4.93	918.70
Hawaii	3.44	3.66	5.55	677.38
Idaho	3.12	3.34	5.10	800.45
Illinois	3.10	3.31	5.06	714.50
Indiana	3.02	3.23	4.95	844.60
Iowa	2.97	3.19	4.88	942.78
Kansas	2.93	3.15	4.84	862.44
Kentucky	2.95	3.17	4.86	890.14
Louisiana	2.96	3.18	4.88	861.63
Maine	3.16	3.38	5.16	1,023.80
Maryland	3.02	3.24	4.96	770.30
Massachusetts	3.04	3.26	4.99	792.74
Michigan	3.07	3.29	5.03	839.20
Minnesota	2.92	3.14	4.82	886.26
Mississippi	2.96	3.18	4.87	946.53
Missouri	2.85	3.07	4.72	909.26
Montana	3.18	3.39	5.18	970.20
Nebraska	3.09	3.31	5.05	821.13
Nevada	3.19	3.40	5.19	657.13
New Hampshire	3.03	3.25	4.97	938.64
New Jersey	2.94	3.16	4.84	823.46
New Mexico	3.05	3.27	5.00	881.15
New York	3.29	3.50	5.33	535.99
North Carolina	3.04	3.26	4.99	872.53
North Dakota	3.10	3.32	5.08	970.94
Ohio	3.03	3.25	4.98	777.95
Oklahoma	2.90	3.12	4.79	1,026.09
Oregon	3.12	3.34	5.09	735.88
Pennsylvania	3.13	3.35	5.11	681.86
Rhode Island	3.09	3.30	5.05	793.87
South Carolina	2.92	3.13	4.81	970.81
South Dakota	3.11	3.33	5.08	990.39
Tennessee	2.96	3.18	4.88	937.25
Texas	2.92	3.14	4.82	895.30
Utah	3.08	3.30	5.04	802.87
Vermont	3.12	3.34	5.10	959.86
Virginia	2.97	3.18	4.88	894.46
Washington	3.22	3.44	5.24	763.27
West Virginia	3.12	3.34	5.10	750.82
Wisconsin	3.06	3.28	5.01	780.60
Wyoming	3.02	3.24	4.96	1,058.13
National Average	\$3.06	\$3.28	\$5.02	\$837.47

*Monthly cost to consumers was calculated by multiplying the price per gallon estimates by gallons of per capita gasoline use by consumers in 2004. This was then multiplied by 12 to obtain an annual estimate. See www.energy.ca.gov/gasoline/statistics/gasoline_per_capita.html for per capita gasoline use by state. The estimate presented in this column is the difference between annual cost in 2016 as compared to annual cost in 2008.

Source: Center for Data Analysis Calculations and California Energy Commission, "U.S. Gasoline Per Capita Use by State 2004," at www.energy.ca.gov/gasoline/statistics/gasoline_per_capita.html.

impact of the energy bill. By 2016, the average cost of gas per gallon nationally will be just over \$5. As a result, consumers will spend an average of \$837 more per year on gasoline in 2016 than in 2008.

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