A GAS TAX INSTEAD OF CAFE

I'm working on a post describing what I think the Big Two and a Half ought to propose on December 2 when they drive their hybrids to DC (in lieu of flying) to beg for money again. As part of that, I will suggest that they ask Congress to levy a stiff gas tax. But since I am getting into more and more discussions with environmentalists who want any bailout to be tied to increased CAFE standards, I'm going to lay out why I think a tax is much better than increased CAFE standards for everyone.

Why CAFE Standards Suck at Achieving their Goal

I'm going to start with the assumption that the goal of CAFE standards is to force auto manufacturers to build more environmentally efficient cars (arguably that's not what it was originally intended to do). It does so with brute force regulation that does not, at the same time, change the actual market-wide interest (or not) in environmental efficiency.

Until gas reached $4 plus this summer (and things are returning—though haven't entirely returned—to where they were now that gas has gotten cheaper again), people calculated "energy efficiency" into their considerations when buying a car in terms of cost of ownership—that is, as one factor among others: how much the car cost, how much monthly loan payments would be, how much maintenance cost, how much insurance cost, and how much gas to run the car cost (this is reflected by the stickers dealers use to sell their cars, which usually describe efficiency both in terms of MPG but also in terms of year gas costs). For most people, efficiency is still a cost issue, and not a benefit per se.

Now consider how that will factor into the choice of a vehicle. For a lot of people, all those cost calculations will be less important than perceived safety or utility arguments. So

if having something that feels like a tank is really important to you, you're going to buy something that feels like a tank and only then consider how much it'll cost you to run your psuedo-tank. The cost calculations will weigh, overall, much less in your consideration.

But if cost of ownership is your primary consideration, then you're going to look at the cheapest cars that meet your basic needs, and pick which one is actually cheapest to run. And so long as energy efficiency remains one cost calculation among others, when people choose to buy based on cost of ownership, you can bet they're going to be choosing to forgo a bunch of other bells and whistles—things like upgraded radios or fancy interiors or navigation devices or things like that—precisely the kinds of bells and whistles that contribute to higher profit margins on cars. In other words, for consumers who are looking at cost of ownership, chances are very good that they're looking for cheap (which, for the auto industry, means low profit margins).

What you don't have, in this calculation, are very many consumers who are interested in environmental efficiency and are willing to pay more for it the way a pseudo-tank driver will pay more to feel powerful on the road. As of May—at a time when rising gas prices were already affecting consumer choices—hybrids made up 2.2 percent of the US market. (I realize this grossly undercounts the people who value energy efficiency, but it's a fair measure of the people who will pay 10% to 25% more solely for efficiency and environmental cache.) That was when gas averaged $3.76 a gallon; it's down to $2.02 a gallon. And manufacturers are still selling those hybrids at a loss or with slim profits, so while those 2.2 percent of consumers will certainly spend more to have an energy efficient car, manufacturers aren't necessarily making more.

All things being equal, the market suggests that manufacturers make their energy efficient cars

cheaply and their gas guzzlers more expensively, because consumers buy energy efficient cars because they're cheap to own, whereas consumers buy trucks or SUVs or sports car because some other feature: speed or pseudo-tank or utility. And so long as gas is cheap, that will remain true.

And CAFE standards don't change this equation at all. They force manufacturers to make more of those cheap energy efficient cars to get their fleet-wide averages down (which cuts into their profitability). And, to some extent, make those cars more palatable to less price-sensitive consumers by adding in things like air bags. But because CAFE standards don't change the market calculations of consumers, CAFE standards don't make energy efficiency more valuable to consumers. CAFE standards basically force manufacturers to put costs into their cars that—unlike, say, safety, for which there has been a dramatic increase of value over the years—consumers don't value. Even while the costs of energy efficiency went down over time, those were still costs with little market value, and therefore costs that cut into the profitability of cars in the short term.

Of course, the increase of gas prices this year dramatically changed that. Fairly quickly (measured, at least, in terms of an industry that things in terms of 3-year cycles), people decided the utility-based reasons they invented for needing a full-sized pickup were less important reasons than getting a car they could afford to drive. All of a sudden, the percentage of people who valued energy efficiency spiked way, way higher than just the people who could buy a hybrid.

This meant that a lot more people who would pay for the bells and whistles that contribute to a profitable car sale also wanted a car that got very good gas mileage.

A Good Gas Tax

One good way to get auto makers to make super-

efficient cars and allow them to remain profitable is to ensure that market conditions continue to value energy efficiency as a benefit unto itself, above any consideration of cost of ownership. And one way to do that is to ensure that gas prices remain high enough—with the kind of stability and predictability that would drive 3-year product cycle calculations—such that consumers continue to place energy efficiency at the forefront of their decision-making about new cars.

You could do this by imposing a gas tax that would keep gas prices up at levels that make energy efficiency a leading factor in choosing cars. Make it a big gas tax, maybe a dollar a gallon, so that the value of energy efficiency remains where it was in August. (Obviously, phase it in, but even at a dollar a gallon gas would still be cheaper than where it was in August.) And use it as a revenue source to accomplish a number of things you need to do to enhance energy efficiency all around.

1. Retire US auto pension debt
2. Continually invest to help all US manufactuers (incl Toyota and Honda and Tesla) retool to meet higher standards (ha! Richard SHelby, got you some cash, I did!!)
3. Invest in public transportation
4. Invest in infrastructure
5. Give credits to middle and working class people to pay their gas bills
6. Give credits to middle and working class people to get out of their gas guzzler and into something efficient

7. As part of 6, implement a recycling program designed to meet European requirements on recycling, which will simultaneously get gas guzzlers off the road while also creating a new green economy

Retiring auto pension debt

Use some gas tax proceeds to help the American car companies become more competitive by eliminating the biggest remaining budget item that they pay that their Japanese competitors don't pay. The more you free up the pension debt with a dedicated tax, the more the American car companies can invest in new technology and—just as importantly—the less chance there is that the Pension Benefit Guarantee Corporation has to pick up that pension obligation.

Continual investment to help all US manufactuers (incl Toyota and Honda and Tesla) retool to meet higher standards

Rather than offer one-time $25 billion packages, a gas tax could fund an ongoing investment fund, both for manufacturers of all kinds (including transplants and smaller manufacturers like Tesla) invest in production. It might also fund a general fund for technology, that would result in technologies that any manufacturer could implement.

Invest in public transportation

Goes without saying.

Invest in infrastructure

Also goes without saying—but also addresses an ongoing problem in that decreased driving has cut into the tax-based road fund as it is. Some of this could go to pay for plug-in and/or hydrogen infrastructure.

Credits for middle class and working class

people

These credits would serve to do two things. In the very short term, it would help people pay for the higher gas prices, so there were some offset of the tax for those who genuinely couldn’t afford it (but obviously not a total offset, since you still need to change the valuation of efficiency). At the same time, part of the revenues from the tax could pay for a program that got people out of old clunkers and into new, efficient cars. (Obviously, this would stimulate the kind of good production we want manufacturers to focus on). This way, you’d increase efficiency in the short term, and keep the customer base at dealers up.

Credits for recycling

But you don’t junk those clunkers. Instead, you have the manufacturers dispose of them, with the expectation that they salvage everything possible as materials (that is, no sales of big engines, but you can sell the steel). You spend some of the funds to offset the costs of a recycling program aiming to match the European standard, with the expectation that new cars would begin to have to meet these standards. Thus, in addition to the credits for new efficient cars, the tax would also lead to a support of a vehicle recycling program.