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# Tradeable Gasoline Rights

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The rapid rise in the price of gasoline has produced calls for tougher fuel economy standards on new cars and trucks. Although reduced gasoline consumption would be good for the environment and for national security, such a regulatory change would be a mistake. A far better approach would be a system of tradeable gasoline rights, or TGRs. These could be distributed in a way that actually raises the income of a majority of households while giving everyone an incentive to reduce gasoline consumption.

In a system of tradeable gasoline rights, the government would give each adult a TGR debit card. The gasoline pumps at service stations that now read credit cards and debit cards would be modified to read these new TGR debit cards as well. Buying a gallon of gasoline would require using up one tradeable gasoline right as well as paying money.

The government would decide how many gallons of gasoline should be consumed per year and would give out that total number of TGRs. In 2006, Americans will buy about 110 billion gallons of gasoline. To keep that total unchanged in 2007, the government would distribute 110 billion TGRs. To reduce total gasoline consumption by 5%, it would cut the number of TGRs to 104.5 billion.

The government could distribute TGRs to reflect geographic differences in driving patterns. Additional TGRs would be distributed to each debit account at the end of each month to avoid problems of expiring rights. Businesses that use trucks would also get TGRs.

A key feature of these gasoline rights is that they are tradeable. Individuals with more TGRs than they need could sell the excess, while those who want to use more gallons than their allocation would have to buy extra TGRs. The gasoline companies could act as clearing houses for these trades, using their gasoline pumps to sell TGRs in the same way that they sell gasoline or to buy TGRs in exchange for the cash needed to purchase gasoline. Other institutions like banks could also trade TGRs for cash. And individuals could of course buy and sell TGRs among themselves by letting others use their card.

The market price of a TGR would depend on the number of TGRs that the government distributed relative to the number of gallons that households would buy if there were no TGR system. The smaller the number of TGRs, the greater would be the price per TGR; the exact price would be determined in the market for these tradeable rights. The money price of gasoline would continue to reflect the world price of oil and the local cost of refining and distribution.

If the price of a TGR turned out to be 50 cents, an individual who buys an extra 20 gallons of gasoline would use up \$10 worth of TGRs. If he avoids the purchase -- by driving less, driving at speeds that use less gas, or driving a more fuel-efficient car -- he could sell the 20 TGRs for \$10.

The 50 cent price of the TGR would have the same incentive effect as a 50 cent gasoline tax. But while a gasoline tax lowers everyone's real income, the TGR system creates winners as well as losers. Someone who receives 800 TGRs for a year but only needs 500 would pocket \$150 by selling his unwanted TGRs. But even such individuals would still face the right incentive: Every extra gallon consumed

would reduce their net cash by 50 cents.

Advocates of a gasoline tax argue that it would produce extra revenue that could be used to reduce the budget deficit or to finance equally large cuts in personal taxes. My own guess is that the increased revenue from a higher gasoline tax would be more likely to finance additional government spending, just as it does in Europe. In any case, it is hard to believe that Congress would now respond to the public's unhappiness over high gasoline prices by enacting a gasoline tax that would raise the price even more.

That aversion to a higher gasoline tax is why tougher mileage standards for new cars is back on the legislative table. They would, however, do virtually nothing to lower the price of gasoline. And if individuals want to economize on gasoline by driving smaller or more fuel-efficient cars, they can do so now without government action. Experience shows that car companies would quickly change the mix of cars that they produce if buyers show an interest in more fuel-efficient vehicles.

Although reducing U.S. gasoline demand could cause some fall in the world oil price, the effect would be quite small. Since U.S. gasoline consumption accounts for only about 15% of total world-wide oil consumption, even a very large 20% reduction in U.S. gasoline consumption would reduce global oil demand by only 3%. Whether this would have any effect at all on the global oil price and therefore on U.S. gasoline prices would depend on whether the oil producing nations cut back on their production. A 3% production fall could leave oil and gasoline prices unchanged.

Higher gas mileage standards would reduce gasoline demand in a very inefficient way by focusing exclusively on the rated mileage of new cars. Separate fuel efficiency standards for each type of vehicle -- one of the options now being considered -- would be even worse because it would provide no incentive to switch to more fuel-efficient cars.

Requiring higher mileage standards on new cars would do very little to reduce total gasoline consumption in the near term because each year's new cars are only about 10% of the total cars on the road. Unlike the system of TGRs that raises the effective cost per gallon, the new car standard would do nothing to change the behavior of owners of existing cars. But the TGR system would cause owners to economize on gasoline by driving fewer miles, driving at speeds that use less gasoline, using tires that improve miles per gallon, and servicing their engines to maintain fuel efficiency. And of course the higher effective cost of gasoline would also cause new car buyers to prefer more fuel-efficient vehicles.

In short, a system of tradeable gasoline rights would be better than either higher taxes or tougher new car regulations. That a majority of households could benefit from the TGR system while all households would have an increased incentive to economize on gasoline is both an economic and a political advantage. It would be an efficient way to reduce gasoline that Congress could actually pass.

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