Leading myths on soaring gasoline prices

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FOR THOSE CONFUSED by the political rhetoric and demagoguery blurring our understanding of gas prices, the following reality check may be helpful:

Assertion: Gas prices are high by historical standards

Facts: The present average price of $3.77 per gallon reflects an annual average increase of real gas prices of less than 1 percent a year since 1981 when gas sold for an inflation adjusted price of $3.04 a gallon. Compare this to a 345 percent increase in educational costs since 1985, and medical costs which have increased at a rate approximately ten times the rate of increases in gas prices.

Assertion: U.S. gas prices are high compared with other developed regions such as Europe.

Fact: Gas now costs as much as $8 and $9 a gallon in European countries.

Assertion: Big oil companies make obscene profits.

Fact: The gross profit margins of oil companies are less than for many other industries, including beverages, electrical equipment, chemicals, and computers.

Assertion: If we imposed special high taxes on oil companies, the price of gas would fall.

Facts: Oil companies earn between 10 and 13 cents a gallon, much of which is recycled back into searching for and developing new sources of oil. If politicians confiscated *all* of big oil's profits, the price of a gallon would fall from $3.77 to $3.65 (assuming that investors would continue to invest capital for a guaranteed return of zero, all oil company employees would agree to work for free, and new sources of oil would be discovered without any effort or expenditure).

Assertion: Oil companies collude in order to set the price of gas at a high level.

Facts: The price of crude oil is set by a world market in oil. Cartels of oil producing countries do engage in blatantly anti-competitive behavior, such as agreeing to restrict production in order to reduce supply and thereby increase the price — behavior which would be criminal if conducted by a corporation in the U.S. However, the member nations of OPEC are not subject to U.S. anti-trust laws.

Assertion: At a price of less than half that paid by Europeans for gas, Americans have an incentive to conserve gas, drive smaller and more fuel efficient cars, and carpool.

Fact: Gas consumption increased last year despite an increase in gas prices.

Assertion: The best way to impose an extra tax on oil companies is to place a special tax on its profits.

Facts: A direct tax on profits increases the cost of production. Since price reflects total costs, such a tax would necessarily result in a proportionate rise in the price of gasoline. A far more efficient tax on oil companies would be a tax imposed at the pump — money which would otherwise go directly to the oil company's coffers. This is called a "gas tax", and European governments impose it to the tune of about $4-5 a gallon, thus raising the cost of a gallon of gas to $8-9 a gallon. If politicians think imposing such a tax would win votes, let them say so directly rather than obfuscating the issue by using such euphemisms as "a windfall-profits tax on big oil."

Assertion: High gas prices would hurt the economy.

Facts: In the short run, higher gas prices would cause economic dislocations. In the long run, a $9 gas price would help our economy as much as it has helped the European economies by providing an incentive to buy and drive fuel efficient cars, renew interest in public transportation and alternative fuels, encourage car-pooling, and reduce our reliance on foreign sources of oil. The revenues from such a tax could be redistributed to taxpayers, particularly the poor, in the form of a reduction in income taxes, leaving everyone better off than before the tax was imposed.

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