One of the leading proposals being floated by Republicans for tax reform is what is called a border adjustment tax. Put simply, it would tax corporate income on imports into the U.S. and leave income from exports tax exempt. The policy argument for it is that it would simplify tax administration for large, multinational companies operating in the U.S., and reduce incentives they currently have to park their profits outside of the U.S. to avoid corporate income tax.

I don’t want to get into the overall merits of the proposal – that’s outside the scope of this blog. But I do want to flag an important and likely outcome of this tax, if it is enacted as currently proposed. It would effectively serve as a carbon tax for petroleum, roughly about 30 to 40 cents per gallon, which is comparable to a carbon tax of $30 to $40 a ton. But unlike the carbon tax floated by eminent conservative leaders that I discussed yesterday, this carbon tax would be regressive.

Why would the border adjustment tax likely serve as a significant carbon tax on petroleum? To understand why requires knowing a little more about how the petroleum market works in the United States. It is true that the U.S. has greatly increased domestic production of petroleum over the past decade, with the boom in production from techniques such as hydraulic fracturing in places like North Dakota. The border adjustment tax will surely increase the incentives for that domestic production, by making imported oil more expensive. However, domestic production generally produces relatively light crude oil. A significant amount of the U.S. oil refinery capacity is built to handle heavier grades of crude oil – which are generally imported from countries such as Canada, Mexico and Venezuela. It is not really feasible to restructure those refineries for the lighter crude – at least not without lots and lots of money (and lots of red tape!). Moreover, the internal pipeline infrastructure in the U.S. does not connect the primary domestic production areas (e.g., North Dakota, Texas) well with some of the major demand centers (such as the Northeast and California) – thus these demand centers will continue to rely on significant imports but at higher prices.

Why is this likely to be regressive compared to the carbon tax proposal I discussed yesterday? That proposal would have directly rebated the proceeds of the carbon tax to all taxpayers on a per capita basis, thus benefitting the poorest Americans most. In contrast the border adjustment tax would simply go into general revenue, where it may (or may not) be spent to help the poorest Americans.

The border adjustment tax is of course a very flawed carbon tax on other grounds –

it isn’t likely to have major impacts on coal (we don’t import any), for instance. But nonetheless, it would be some form of a carbon tax, and that on the margin probably would create more of an incentive for consumers to move to higher-mileage cars. Though I doubt that’s what the Republicans have in mind when they propose it.

In writing up this blog post, I drew on four analyses of the oil markets (#1, #2, #3 (subscription required for the third one), #4). I have some additional reasons I think that the tax may well increase gas prices. The Koch brothers have come out in opposition to the border adjustment tax. (Indeed they financed the fourth analysis I relied on!) They have investments in refineries that process heavy crude oil – the refineries that are most likely to be put under pressure from the border adjustment tax. (For more details, see my discussion of those investments, their history, and the role they played in encouraging the Koch brothers to fight California’s efforts to control greenhouse gas emissions, at footnote 66 in my article here). One last caveat to the analysis is that to the extent the U.S. dollar’s value changes in response to the tax, that may offset some of the impacts I’ve identified here.