

The Daily Dish

Policy Versus Politics, The Carbon Tax Edition

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Eakinomics: Policy Versus Politics, The Carbon Tax Edition

Since the ascendency of the Green New Deal on the progressive left, there has been a renewed interest in carbon taxes and where they fit in any proposed policy architecture. Interest in carbon taxes is not new. A well-designed carbon tax can help to achieve other tax reform goals and is much more efficient than the command-and-control regulatory approach. But the idea that a carbon tax is imminent seems overstated; a well-designed carbon tax still faces some severe political headwinds.

What does a well-designed carbon tax look like? In brief, it is economy-wide (carbon is carbon regardless of source), imposed as far upstream as possible (at the well-head, mine, or place of import), is "border-adjusted" so that imports and domestic goods face the same tax for the same carbon content, and has a rate that starts low enough to be economically feasible but rises fast enough to meet climate objectives. What could go wrong? Everything.

Despite the chatter, climate policy (in general) and carbon taxes (in particular) are still an issue for the elites. The recent "yellow vest" protests in France over a gas tax hike are a good example of the populist response when the elites decide to make a basic necessity more expensive for policy goals that do not have widespread buy-in. Switching the carbon tax away from being an economy-wide, upstream tax to a fee on carbon emitters would transfer the policy into a "polluter pays" system. That might be politically more palatable, but the economic and administrative advantages would be lost. Oh, and remember the response when the House of Representatives floated a plan to "border-adjust" the corporation tax as part of tax reform? The screaming will be no more subdued for a carbon tax.

A well-designed carbon tax would replace the regulatory approach. It would involve federal

pre-emption of carbon regulation under the Clean Air Act, Clean Water Act, Endangered Species Act, National Environmental Policy Act, and myriad other laws. The fact that carbon-intensive products would be relatively more expensive would give incentives to shift away from those products and to innovate products that have lower carbon content. If you have no faith in the power of economic incentives — that is, if you are part of the progressive left — you will not believe that the carbon tax will really work. Those politics say that it is better to have the carbon tax and the regulatory approach.

Finally, a well-designed carbon tax is revenue neutral, using the funds raised by the carbon tax to permit lower tax rates on the return to work and the earnings from capital investments. That mix is essential to have both economic growth and reduced emissions. But the idea that the little guy should pay the carbon tax so that businesses get cheaper labor and capital is easily subject to political demagoguery. An alternative approach that is perhaps politically more appealing is the so-called "carbon dividend" — giving the money back in a equal-sized check to every American. But the idea that the one-percenters and low-income population should get the same check will last about a nanosecond, and once the checks are a regular part of the entitlement state they are unlikely to go away even if the carbon-tax revenue does.

There are myriad points where the policy and politics of a well-designed carbon tax collide. Getting a carbon tax might not be that hard. Getting one worth having is a completely different issue.