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## **Tax Day Prompts Rethinking on Climate Policy**

It's tax time, and millions of Americans will steel themselves to send Washington more of their hard earned money than they estimated they'd have to. It may feel galling, perhaps because the benefits of our taxes often go unnoticed. We come to expect drivable roads, clean water, responsive police and fire services, benefit payments and health care for our parents or grandparents, and even a world where no nation dares attack us. So, when elected officials propose a new tax, the normal responses range from "what for" to "hell, no."

This anti-tax sentiment sometimes leads policymakers to dream up complicated schemes to collect revenues without seeming to tax anyone. That's the case, for example, with the convoluted cap-and-trade strategy for addressing climate change. Climate, at least, is a cause which passes the "what for" test. But there's a much better way to deal with it that might not inspire a "hell, no" reaction: apply a fee to all forms of energy based on how much carbon dioxide and other greenhouse gases each releases into the climate, and then recycle the revenues as cuts in payroll and other taxes.

Such a revenue-neutral carbon-based tax has some surprising support, especially compared to the cap-and-trade alternative supported by some industries and by most of Wall Street -- who unsurprisingly want to get their hands on the markets that would trade the scheme's "permits" for producing greenhouse gases. In fact, a recent survey conducted by Hart Research found that Americans prefer a carbon tax over cap-and-trade by a two-to-one margin.

Some politicians are catching up with the people. Following the lengthy and contentious health care debate, officials from Sen. Lindsey Graham to Interior Secretary Ken Salazar have declared the cap and trade bill "dead." This changing political landscape has led even diehard cap-and-trade supporters such as Senator John Kerry to rethink the approach. And with the end of the Democrats' filibuster-proof majority in the Senate, almost all of Washington now see that only a bipartisan effort can pass climate change legislation. At least, we may be over the first hurdle: To draw support from both parties, it has to earn the public's support.

The new political viability of a carbon-based tax certainly reflects, in important part, its

ability to recycle its revenues back into the pockets of Americans. So we end up taxing what we want less of, namely greenhouse gas emissions, and cutting the tax burden on what we want more of, such as people working.

Beyond that also lies its powerful appeal as the most effective way to beat climate change: by setting a certain and stable price on greenhouse gas emissions -- which neither cap-and-trade nor EPA regulation is designed to do -- a carbon-based tax creates the economic incentives for businesses to develop the new fuels and technologies we need to control global warming, and the incentives for the rest of us to adopt those new fuels and technologies.

A few diehards continue to defend emission-trading markets, and some others want to go forward with the system in a more limited way. But in all of its forms, cap-and-trade depends on financial markets to trade its permits to produce greenhouse gases; and as Europe's current experiment with this approach demonstrates, those markets produce volatile prices, large-scale financial speculation, and a troubling vulnerability to manipulation. In Europe, these permit markets also have produced a range of new financial derivatives. Following the pivotal role such risky instruments played in the 2008-2009 financial meltdown, the last thing U.S. taxpayers should accept is another round of trillion-dollar Wall Street betting, this time based on energy instead of housing, and likely to eventually need another huge taxpayer bailout.

Even if the financial shenanigans that accompany cap-and-trade were somehow banished -- and none of the new proposals for "cap-and-trade light" manage that trick -- the scheme will ultimately fail to provide taxpayer value by setting us on a true path to clean energy. That's because, once again, cap-and-trade systems are incapable of creating a stable price for carbon. Instead, the price moves up and down with energy demand - an average of more than 20 percent per-month in Europe's version -- necessarily weakening people's impulses to prefer more climate-friendly fuels and technologies. The result is that greenhouse gas emissions continue to rise in Europe despite cap-and-trade.

Now, compare that result with the record in Sweden, which enacted a carbon tax 19 years ago. Today, Sweden's greenhouse gas emissions are 8 percent lower than they were in 1990, while the Swedish economy has expanded 45 percent, after inflation.

To be sure, some cap-and-trade advocates are trying to address the scheme's most obvious shortcomings. Senators Maria Cantwell and Susan Collins have introduced a "cap-and-dividend" plan that would auction emission permits to major polluters each month, allow only those polluters to trade the permits among themselves, limit the volatility in the prices of those trades, and return 75 percent of the proceeds to taxpayers. It's real progress over the Waxman-Markey bill from the House. But it won't prevent shadow markets in permit derivatives from springing up as they have in Europe, and significant price volatility remains.

These deficiencies help explain why most economists and climate scientists, along with growing numbers of environmentalists and average Americans, prefer a simple, straightforward carbon tax that recycles its revenues to the other options on the table. What U.S. taxpayers need today, especially as tax day looms, is a genuine and truthful public debate about the real options available to address climate change. Once they get that, a genuine, bipartisan consensus should emerge around the best response, a revenue-neutral carbon-based tax.

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