Carbon tax 'dividends' open a Pandora's box of problems

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Carbon tax advocates recently received a huge boost from a wide group of famous economists who signed a letter supporting a carbon tax that sends revenues directly to citizens and shrinks redundant environmental regulation. A tax of $40 per ton is estimated to generate $2,000 in the first year for a family of four and rebates would rise with tax rates. Signers include previous chairs of the Council of Economic Advisors and of the Federal Reserve and countless Nobel laureates.

Despite assurances, the “dividend” program is controversial among economists interested in having a more efficient, but limited, government.

The tax “dividend” proposal is intriguing theoretically, but it would expose the carbon tax to the machinations of politics as discussed in my “The Perils of Carbon Taxes” just published in the Cato Institute’s "Regulation." My paper reveals that the “dividend” program opens a Pandora’s box of problems for advocates of limited government.

Carbon tax advocates argue that carbon taxes are necessary to limit climate change. Rather than reduce other taxes that are more economically distortionary, resulting in a “revenue neutral” outcome, this proposal expands tax collection.

The "dividend" program creates a new income-redistribution arrangement that collects taxes on fossil fuels and then sends those dollars to citizens in a political game of expanding the welfare state. New redistributive promises quickly become entitlements, expand and are nearly impossible to unwind.

Tax collection rises without a healthy debate on which ongoing spending and tax programs should be reformed, downsized or eliminated. The “dividend” program simply adds a new tax source onto our existing tax code. More tax revenue, more government.

The U.S. Treasury estimated that a carbon tax that started at $49 per metric ton of carbon dioxide and increased to $70 in 2028 would generate net revenues of $194 billion in the first year of the tax and $2.2 trillion over the 10-year period.

The impending expected escalation of government debt will also undoubtedly encourage many attempts at siphoning off carbon tax revenues for other uses. The Congressional Budget

Office projects that federal deficits will average $1.2 trillion per year and total $12.4 trillion over the 2019–2028 period.

Much of the spending growth reflects increases for Social Security, Medicare and interest on government debt. A great many politicians, interest groups and voters can be expected to seek new tax revenues rather than cut or reform spending programs to fund this widening budgetary gap.

The carbon tax "dividend" proposal is likely to become the best friend of those believing government under-taxes rather than over-spends.

Government spending and tax programs are unlikely to receive much scrutiny as long as new tax revenues keep flowing to Washington. Carbon tax "dividends" appear to fit this profile since it is very unlikely to foster a holistic discussion about the proper role of government.

A carbon "dividend" program essentially closes discussion of which taxes will be swapped, reduced or eliminated that harm economic growth and job creation. Moreover, the "dividend" program encourages citizens to believe (incorrectly) they bear little to no cost themselves for checks from the U.S. government, thus fostering greater demands for government expansion.

Revenue neutrality of course will not make government hyper-efficient, but it will provide a fixed pool of funds for policy advocates to draw from. Think tanks have devoted much energy to proposing how best to cut wasteful government programs. These are excellent starting points for improving the efficiency of government.

Carbon tax proponents who truly believe it is essential for mitigating the effects of climate change should be willing to negotiate a tax swap that promotes a more efficient government. Proponents unwilling to negotiate are probably more interested in growing tax revenue than decreasing greenhouse gas emissions.

Michael L. Marlow is professor of economics at California Polytechnic State University. His recent article, "The Perils of a Carbon Tax," appears in the current issue of Regulation and is based on his white paper "A Carbon Tax That Constrains Government," produced for the Alliance for Market Solutions.