The Heritage Foundation
LEADERSHIP FOR AMERICA

BACKGROUNDER

No. 2720 | AUGUST 21, 2012

A Carbon Tax Would Harm U.S. Competitiveness and Low-Income Americans Without Helping the Environment

Derrick Morgan

Abstract
Supporters of a new carbon tax are using arguments aimed at conservatives (it can be revenue neutral) and liberals (it can help the environment) alike. But even if one concludes that carbon dioxide and other greenhouse gases are leading to increased temperatures—and there is robust debate and far from a public consensus on the magnitude of man-made warming, particularly among conservatives—a carbon tax would (1) do next to nothing to lower global temperature, (2) harm American manufacturing competitiveness, (3) create a new revenue stream based on behavior modification, and (4) harm low-income Americans. Energy supplies can be delivered and new supplies created through the private sector rather than through mandates, regulations, taxes, and subsidies ordered by government.

This paper, in its entirety, can be found at **http://report.heritage.org/bg2720**

Produced by the Department of Domestic and Economic Policy

The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002
(202) 546-4400 | heritage.org

In America's struggling economy, fossil fuel production stands out as a bright spot. Currently, 9,000,000 Americans work in the oil and natural gas industry,[1] and another 550,000 Americans work in coal mining.[2] Wages for these jobs are well above average,[3] and production of fossil fuels, particularly natural gas, is booming in places like North Dakota.[4]

The economic gains being made now have the potential to be long-lasting; the United States has the largest reserves of fossil fuels—oil, coal, and natural gas—in the world. (See Chart 1.) These gains, however, are threatened by unfriendly energy policy from Washington. President Barack Obama and his allies in Congress continue to block fuel production on federal lands and offshore,[5] have stopped a pipeline project that would increase North American–sourced petroleum products,[6] are severely limiting coal production,[7] and continue to allow the Environmental Protection Agency to regulate carbon dioxide (CO_2).

The left has argued for decades that using fossil fuels is bad for the country.[8] Initially, their concerns involved direct public health concerns such as oil spills, mercury, and other toxic pollutants.[9] Their attack

Key Points

- Despite claims made by supporters, a new carbon tax likely would not be revenue neutral and would not help the environment.
- Congress and the President should reject a new carbon tax, which would have little environmental impact, harm manufacturing, be another tax seeking to control behavior, and disproportionately harm the poor.
- Congress and the President should work to stop EPA regulations of greenhouse gases, which will hurt the economy but have no appreciable impact in reducing global greenhouse gas emissions.
- Congress and the President should work to reform the tax system so that the revenue to fund necessary government operations is raised in ways that cause the least possible economic damage and do not pick winners and losers with preferential or punitive policies.
- Energy, like other sectors, should not become a playground for connected lobbyists to collude with government for special treatment.

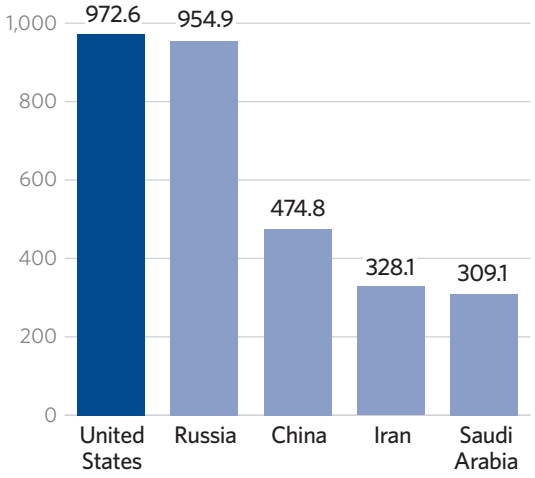
on fossil fuels has increased in recent years because fossil fuels are by far the biggest contributor to U.S. greenhouse gas emissions (GHGs), thought by some to lead to global warming.[10] To limit GHG emissions, President Obama pushed a cap-and-trade energy bill in the 111th Congress that passed the House but was halted in the Senate. The President is now moving full speed ahead with regulation of GHGs by the Environmental Protection Agency (EPA) under the Clean Air Act.

Although cap-and-trade was rejected by the Senate and the American people as a new energy tax, some have championed the idea of a new carbon tax, with arguments aimed at conservatives (it can be revenue neutral) and liberals (it can help the environment) alike.[11] A new federal carbon tax would likely fail to achieve either goal while further slowing America's recovery.

CHART 1

U.S. Has Largest Fossil Fuel Reserves

TOP FIVE NATIONS, IN BILLIONS OF BARRELS EQUIVALENT



Source: Congressional Research Service, "U.S. Fossil Fuel Resources: Terminology, Reporting, and Summary," November 30, 2010, Table 5, p. 16, http://epw.senate.gov/public/index.cfm?FuseAction=Files.view&FileStore_id=04212e22-c1b3-41f2-b0ba-0da5eaead952 (accessed August 2, 2012).

B 2720 heritage.org

Carbon Tax and Cap-and-Trade: What's the Difference?

Cap-and-trade and a carbon tax are two ways to limit greenhouse gas emissions. If planners knew the market's behavior perfectly, then a cap-and-trade system and carbon tax could put the same price on emissions, achieving exactly the same effect—reduced emissions and higher prices for fossil fuel–powered energy and products. Planners cannot know

1. American Petroleum Institute, "Policy and Issues" website, http://www.api.org/policy-and-issues/policy-items/jobs/energy-works.aspx (accessed August 9, 2012).
2. "The Economic Contributions of U.S. Mining in 2008," PriceWaterhouseCoopers for the National Mining Association, October 2010, p. 4, http://www.nma.org/pdf/economic_contributions.pdf (accessed July 17, 2012).
3. See, e.g., U.S. Department of Labor, Bureau of Labor Statistics, Quarterly Census of Employment and Wages, "Private Industry by Six-digit NAICS Industry and Government by Level of Government, 2010 Annual Averages: Establishments, Employment, and Wages, Change from 2009," http://www.bls.gov/cew/ew10table2.pdf (accessed August 9, 2012).
4. Brandon Stewart, "A Fracking Miracle: North Dakota's Bakken Boom," The Heritage Foundation, The Foundry, June 19, 2012, http://blog.heritage.org/2012/06/19/a-fracking-miracle-north-dakotas-bakken-boom-video/.
5. Nicolas Loris, "Ten Actions Congress Can Take to Lower Gas Prices," Heritage Foundation *Backgrounder* No. 2689, May 31, 2012, http://www.heritage.org/research/reports/2012/05/ten-actions-congress-can-take-to-lower-gas-prices.
6. Nicolas Loris, "Obama's 'Forced' Keystone Decision Rejects Jobs, Energy and Logic," The Heritage Foundation, The Foundry, January 18, 2012, http://blog.heritage.org/2012/01/18/obama%E2%80%99s-forced-keystone-decision-rejects-jobs-energy-and-logic/; Nicolas D. Loris, "Keystone a Key Ingredient Missing from Obama's Economic Recovery Recipe," Heritage Foundation *WebMemo* No. 3472, January 25, 2012, http://www.heritage.org/research/reports/2012/01/keystone-pipeline-rejection-and-obamas-economic-recovery-plan.
7. Nicolas Loris, "The Assault on Coal and American Consumers," Heritage Foundation *Backgrounder* No. 2709, July 23, 2012, http://www.heritage.org/research/reports/2012/07/the-assault-on-coal-and-american-consumers.
8. See, e.g., "Greenpeace Members Arrested in Protests of Oil Dependence," *Los Angeles Times*, September 30, 1990 ("Greenpeace said the purpose of the protest was to call attention to the nation's 'overdependence' on fossil fuels and a need for an energy policy based on clean, renewable resources.").
9. See, e.g., "Earth Day: The History of a Movement," Earth Day Network website, http://www.earthday.org/earth-day-history-movement/ (accessed July 25, 2012).
10. U.S. Environmental Protection Agency, *Inventory of Greenhouse Gas Emissions and Sinks: 1990–2010*, Table ES-2, p. ES-4, April 15, 2012, http://www.epa.gov/climatechange/Downloads/ghgemissions/US-GHG-Inventory-2012-Main-Text.pdf.
11. Although some might appreciate the revenue effects of a carbon tax, its primary purpose seems to be to regulate energy production.

such information, so the proposals look to achieve different goals: A cap-and-trade system includes a strict limit on the amount of GHGs emitted but unclear costs, while a carbon tax imposes higher known costs but unclear emissions reductions.

Under a cap-and-trade system, those who wish to emit must purchase an allowance by auction or from others who have allowances to sell. In the Waxman–Markey bill,[12] for example, allowances would be distributed to utilities (to soften the increase in rates), manufacturers (to protect domestic industry), and others, including environmental groups that theoretically would use the proceeds to improve the environment. Other allowances were to be auctioned to the highest bidder, thus revealing, in theory, how much the "right to emit" costs.

A carbon tax approaches the issues from a different perspective. In that system, the "right to emit" is not limited by capping the amount of GHGs that are emitted. Instead, anyone who wishes to emit must pay a tax. Since it will be more expensive to emit than before, GHGs will decline, albeit by an unknown amount: The higher the tax, the more the emissions will decline. Many environmentalists prefer the cap-and-trade system because the cap ensures that the environmental purposes of the act are met.

Each of these mechanisms is effectively a tax, or fee, on emitting GHGs. To create momentum for its passage, proponents of cap-and-trade argued to conservatives that it would do less damage to the economy than EPA regulation would. Now others are saying that a carbon tax could be better still. But as one scholar at the American Enterprise Institute put it, "Carbon taxes might be 'better' than cap-and-trade or regulations, but then, in a train-wreck, losing a hand is better than losing a forearm, which is better than losing an entire arm. Most would rather skip the wreck."[13] Congress seems closer to stopping EPA regulation[14] than it does to adopting a carbon tax, especially considering that conservatives successfully attacked cap-and-trade by calling it an energy tax.

Enacting a carbon tax is an unwise policy and against conservative principles because, among other reasons, a carbon tax would:

- Do next to nothing for GHG emissions and the environment,
- Harm American manufacturing competitiveness,
- Create a new revenue stream based on behavior modification, and
- Hit low-income Americans especially hard.[15]

No Environmental Benefit

Even if one assumes that rising levels of carbon dioxide in the atmosphere lead to higher global temperatures, a carbon tax in the United States that reduces emissions domestically would have zero direct effect on foreign emissions if we acted alone. In fact, unilateral action by the U.S. would have very little effect on total global emissions.

The EPA analyzed a cap-and-trade proposal and projected global CO_2 concentrations in a baseline and under legislation, demonstrating the effects graphically.[16] (See Figure 1.) The Administrator of the EPA testified on July 7, 2009: "I believe the central parts of the [EPA] chart are that U.S. action alone will not impact world CO2 levels...."[17] The analysis showed that even if the U.S. adopted stringent carbon caps under that legislation[18] and the international

12. The American Clean Energy and Security Act, H.R. 2434, 110th Congress.
13. Kenneth P. Green, "Dissecting the Carbon Tax," American Enterprise Institute, July 7, 2011, http://www.aei.org/article/dissecting-the-carbon-tax/ (accessed July 17, 2012).
14. The tax has to be high to meet the goals of the environmental left, which has shown very little interest in the carbon tax replacing uneconomical regulations. The House voted 255–172 on April 7, 2011, to prevent EPA regulation of GHGs, and 47 Senators voted on June 10, 2010, to disapprove of EPA regulations under the Congressional Review Act, S.J. Res 26.
15. Taxes on businesses are merely collected from businesses but are ultimately paid by some combination of the businesses' owners, customers, or workers. This paper does not address that argument; instead, it concentrates on the initial effects of the tax, which will be felt by consumers, at least in the near term.
16. S. 2191, the Lieberman–Warner bill. See U.S. Environmental Protection Agency, Office of Atmospheric Programs, "EPA Analysis of the Lieberman–Warner Climate Security Act of 2008: S. 2191 in 110th Congress," March 14, 2008 (updated May 5, 2008), http://www.epa.gov/climatechange/Downloads/EPAactivities/s2191_EPA_Analysis.pdf (accessed July 17, 2012).
17. News release, "Jackson Confirms EPA Chart Showing No Effect on Climate Without China, India," Committee on Environment and Public Works, U.S. Senate, July 7, 2009, http://epw.senate.gov/public/index.cfm?FuseAction=Minority.PressReleases&ContentRecord_id=564ed42f-802a-23ad-4570-3399477b1393&Region_id=&Issue_id (accessed August 15, 2012).
18. A cut of 40 percent by 2030 with allowance prices reaching up to $220 per ton by 2050.

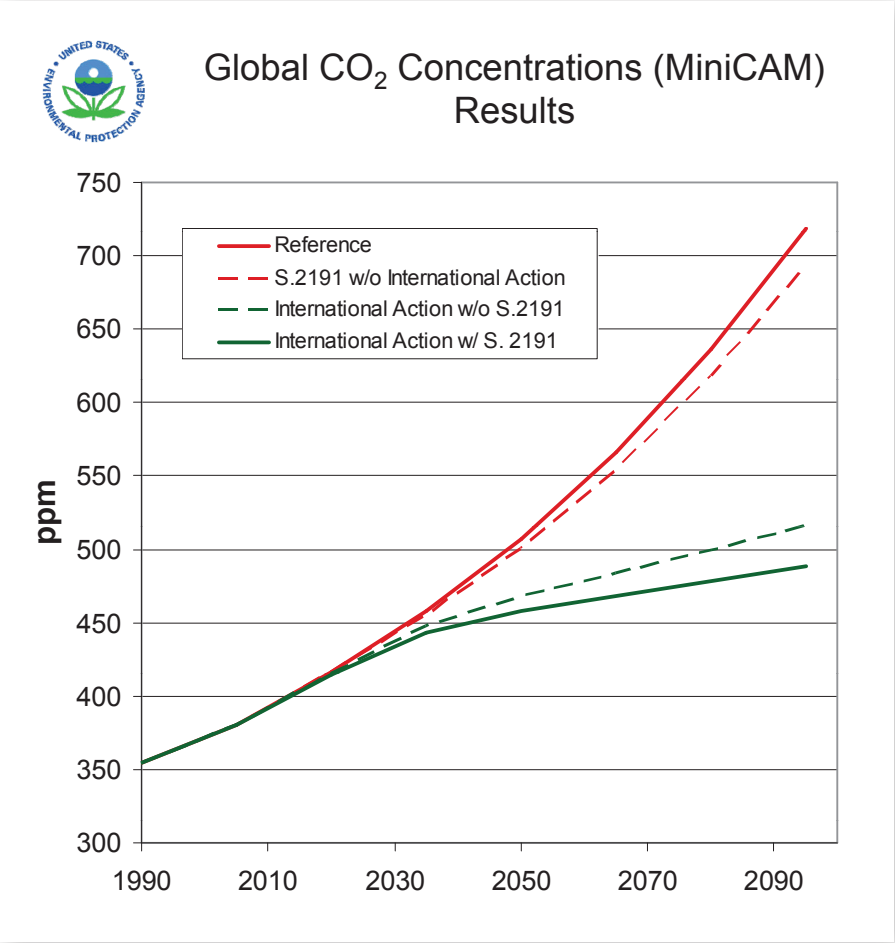


FIGURE 1

EPA Analysis Shows Climate-Change Bill Would Have Little Effect on CO_2 Concentrations

The chart at left was prepared by the EPA in 2008 as part of their analysis of S. 2191, also known as America's Climate Security Act of 2007.

The chart shows the EPA's projected global CO_2 concentrations, in parts per million (ppm). The top line, labeled "Reference," shows the baseline projections, and the line underneath it shows projections based on the passage of S. 2191 but without any additional action from other countries.

Accompanying the chart is an annotation that reads, "Assuming the international community adopts no additional policies or measures, the global CO_2 concentrations in 2095 are estimated to be 694 ppm, which is 25 ppm lower than the reference case."

Source: U.S. Environmental Protection Agency, "EPA Analysis of the Lieberman-Warner Climate Security Act of 2008," p. 192, March 14, 2008, http://www.epa.gov/climatechange/Downloads/EPAactivities/s2191_EPA_Analysis.pdf (accessed August 16, 2012).

community did not, global CO_2 concentrations would decrease 25 parts per million (with concentrations equaling 694 ppm in 2095). International action, by contrast, would decrease concentrations by 202 ppm.

Just as in a unilateral U.S. cap-and-trade system, a unilateral U.S. carbon tax would likely further *increase* foreign emissions because of a phenomenon called "carbon leakage." As energy-intensive industry relocates from the United States to other nations such as Mexico, Vietnam, or China (already the world's largest emitter of greenhouse gases), GHG emissions and toxic pollutants could increase more than they would if those industries remained in the United States.[19]

Unilateral action by the United States to tax carbon emissions is unwise because it would not achieve its stated environmental goal: material reduction of global GHG emissions.

Harm to Manufacturing

While some may believe that the United States is a post-industrial power, it is still the world's top

19. See Alliance for American Manufacturing, *An Assessment of Environmental Regulation of the Steel Industry in China*, March 2009, p. 59, http://www.americanmanufacturing.org/wordpress/wp-content/uploads/2009/03/chinaenvironmental-report-march-2009.pdf (accessed July 17, 2012).

China's Role and Benefits of Growth

China's role in emitting GHGs can hardly be overstated. From 2000–2008, its emissions doubled from 3.4 gross tons (Gt) to 7 Gt of CO_2. By contrast U.S. CO_2 emissions remained about 5.7 Gt in 2000 and 2008.[20] China overwhelmingly relies on coal for electricity generation—accounting for about half of the world's annual coal consumption.[21]

For those who lament an increase in global GHG emissions, China's carbon-footprint increase in the past few decades has been a disaster, but the Chinese people have seen a nearly sixfold increase in per capita gross domestic product (GDP) from 1990 to 2011.[22] Hundreds of millions of Chinese have been lifted from poverty thanks to agricultural and free-market reforms that have led to economic development.[23]

It is important to remember that environmental policy must ultimately be good for people, any country's most important resource. Moreover, economic growth also creates the wealth necessary for countries to make real environmental improvements in the long run.[24]

manufacturer[25] (although China is gaining), with manufacturing accounting for 12.2 percent of U.S. GDP.[26]

Proponents of cap-and-trade acknowledged that a price on GHG emissions would negatively affect domestic manufacturing unless the cost was fully and permanently offset. Additionally, to offset the impact on manufacturing fully and permanently would be to negate the desired environmental impact of the policy (make it more expensive to emit GHGs and therefore reduce GHGs).

To make up for the impact on manufacturers, the Waxman–Markey cap-and-trade bill gave temporary free allowances to manufacturers to ease the impact of the cap on emissions. Nearly all manufacturers use energy, and for those that emit greenhouse gases in significant quantities, such as steelmakers, a tax on a major input would be devastating. Moreover, a tax on carbon would also affect those who use carbon-intensive fuels for feedstocks, as is the case in the chemical and fertilizer industry. The recent natural gas boom is encouraging more investment in these industries,[27] but a carbon tax would make such investments much less appealing.

During the cap-and-trade debate in 2009, the National Association of Manufacturers and the National Black Chamber of Commerce commissioned studies looking at the effect of carbon caps on manufacturing and found that hundreds of thousands of manufacturing jobs would be lost.[28] A Heritage Foundation

20. Sergey Paltsev, Jennifer Morris, Yongxia Cai, Valerie Karplus, and Henry Jacoby, "The Role of China in Mitigating Climate Change," MIT Joint Program on the Science and Policy of Global Change *Report* No. 215, April 2012, p. 4, https://www.gtap.agecon.purdue.edu/resources/download/5824.pdf (accessed August 9, 2012).
21. Ibid., p. 3.
22. U.S. Department of Agriculture, Economic Research Service, "The International Macroeconomic Data Set," updated July 5, 2012, http://www.ers.usda.gov/data-products/international-macroeconomic-data-set.aspx (accessed July 30, 2012).
23. See, e.g., Yasheng Huang, *Capitalism with Chinese Characteristics: Entrepreneurship and the State* (New York: Cambridge University Press, 2008).
24. See Ben Lieberman, "A Free Economy Is a Clean Economy: How Free Markets Improve the Environment," Chapter 4 in Terry Miller and Kim R. Holmes, *2011 Index of Economic Freedom* (Washington: The Heritage Foundation and Dow Jones & Company, Inc., 2011), pp. 53–60, http://thf_media.s3.amazonaws.com/index/pdf/2011/Index2011_Chapter4.pdf.
25. United Nations, "National Accounts Main Aggregates Database," 2010, http://unstats.un.org/unsd/snaama/selbasicFast.asp (accessed July 17, 2012).
26. 2011 figures. See Donald D. Kim, Teresa L. Gilmore, and William A. Jolliff, "Annual Industry Accounts: Advance Statistics on GDP by Industry for 2011," U.S. Department of Commerce, Bureau of Economic Analysis, *Survey of Current Business*, Vol. 92, No. 5 (May 2012), Table E, p. 12, "Value Added by Industry Group as a Percentage of Current-Dollar GDP," www.bea.gov/scb/pdf/2012/05%20May/0512_industry.pdf.
27. Mike Shannon, Paul Harnick, and Tom Meike, "The Future of the US Chemical Industry," *Reaction Magazine*, Seventh Edition (June 2012), pp. 8–11, http://www.kpmg.com/global/en/issuesandinsights/articlespublications/reaction/pages/the-future-of-the-us-chemical-industry.aspx (accessed August 9, 2012).
28. American Council for Capital Formation and National Association of Manufacturers, "An Analysis of the Waxman–Markey Bill 'The American Clean Energy and Security Act of 2009' (H.R. 2454) Using the National Energy Modeling System (NEMS/ACCF-NAM 2)," http://accf.org/wp-content/uploads/2009/10/accf-nam_study.pdf (accessed August 9, 2012), and CRA International, "Impact on the Economy of the American Clean Energy and Security Act of 2009 (H.R.2454)," August 2009, http://www.nationalbcc.org/images/stories/documents/CRA_Waxman-Markey_Aug2008_Update_Final.pdf (accessed August 9, 2012).

study reached the same conclusion.[29] A carbon tax would raise prices on energy inputs for manufacturing and therefore destroy manufacturing jobs.

A carbon tax would especially hurt states with higher concentrations of manufacturing and that use coal for electricity generation. The Heritage Foundation developed the Manufacturing Vulnerability Index, a list of states with their combined manufacturing prevalence and coal electricity generation, highly concentrated in the Midwest.[30] These states have substantial infrastructure for manufacturing and coal-powered electricity generation that would be hit especially hard. A transition to other power-generation sources and economic activities would be very costly to these already hurting states.

While proponents of a carbon tax explain that they could impose an adjustment tax on goods from countries without a carbon tax to help level the playing field, such an action could precipitate a trade war. Moreover, it would place U.S. manufacturers that export from the United States to other markets at a disadvantage when compared to manufacturers that produce in nations without GHG controls.

A new carbon tax should not be imposed because it would harm U.S. manufacturing, destroying the livelihood of too many Americans who want to go to work producing products for the world.

WHILE SOME HAVE ASSERTED THAT THEY CAN BE "AGNOSTIC" ABOUT WHETHER HUMAN ACTIVITY IS CONTRIBUTING SIGNIFICANTLY TO GLOBAL WARMING AND STILL WANT TO TAX CARBON, CHOOSING TO PLACE A TAX ON CARBON IS AN ENDORSEMENT OF THE THEORY THAT MAN-MADE EMISSIONS OF GHGS HAVE A SIGNIFICANTLY HARMFUL EFFECT ON THE ENVIRONMENT.

New Opaque Tax Easy to Raise and Seeks to Manipulate Behavior

Creating an entirely new federal revenue stream does not usually end up well for taxpayers, even if its initial goals are modest. Data from the Tax Foundation show that the marginal income tax rate, for example, was 1 percent for married filers making less than $448,759 per year in 1914 (adjusted for inflation).[31] The highest marginal rate at the time was 7 percent.[32] Over the years, the highest marginal rate was raised to nearly 70 percent as recently as 1979 and 91 percent in 1963.[33] Currently, the highest bracket is 35 percent, and the lowest bracket is 10 percent.[34] Reducing marginal income tax rates is a great way to encourage growth and prosperity, as Presidents as diverse as Ronald Reagan and John Kennedy have recognized.

Some economists eager to reduce taxes and encourage economic growth have thought that revenue from a new carbon tax could be used to reduce other harmful taxes on capital and investment. But because the carbon tax hits the poor disproportionally, it is likely that revenue from the tax will be used to alleviate its impact on the poor or for some other purpose rather than to cut other taxes in an economically simulative way.

The Heritage Foundation has published the principles for tax reform and has noted that, above all, "[t]axes should raise the revenue to fund necessary government operations in ways that cause the least possible economic damage"[35] and that

29. Nicolas Loris, "Waxman–Markey Cap and Trade's Biggest Losers: Manufacturing," The Heritage Foundation, The Foundry, June 25, 2009, http://blog.heritage.org/2009/06/25/waxman-markey-cap-and-trade%E2%80%99s-biggest-losers-manufacturing/.
30. Nicolas Loris, "Manufacture This: 10 Democrats Express Concern over Cap and Trade," The Heritage Foundation, The Foundry, August 7, 2009, http://blog.heritage.org/2009/08/07/manufacture-this-10-democrats-express-concern-over-cap-and-trade/.
31. Tax Foundation, "U.S. Federal Individual Income Tax Rates History, 1913–2011 (Nominal and Inflation-Adjusted Brackets)," September 9, 2011, http://taxfoundation.org/article/us-federal-individual-income-tax-rates-history-1913-2011-nominal-and-inflation-adjusted-brackets (accessed July 16, 2012).
32. Ibid.
33. Ibid.
34. Ibid.
35. "Solutions for America: Tax Reform," The Heritage Foundation, August 17, 2010, http://www.heritage.org/research/reports/2010/08/tax-reform. See also Stuart M. Butler, Alison Acosta Fraser, and William W. Beach, eds., *Saving the American Dream: The Heritage Plan to Fix the Debt, Cut Spending, and Restore Prosperity*, The Heritage Foundation, 2011, p. 35 ("The federal tax system need not be so complex or damaging to our economy, nor should it be."), http://savingthedream.org/about-the-plan/plan-details/.

government should avoid "picking winners and losers with preferential or punitive policies."[36]

While some have asserted that they can be "agnostic" about whether human activity is contributing significantly to global warming and still want to tax carbon, choosing to place a tax on carbon is an endorsement of the theory that man-made emissions of GHGs have a significantly harmful effect on the environment. In effect, such backers of the carbon tax would treat using fossil fuel resources to heat or cool your home, turn on your lights, drive your car, and charge your cellular phone the same as they would treat using disfavored goods such as alcohol and cigarettes.

Using the tax code to discourage behavior has been encouraged by *NFIB v. Sebelius*, the health care case in which the Supreme Court held that the federal government has broad authority to tax, including to compel behavior.[37] Some localities have already imposed taxes on plastic bags and soft drinks.[38] Conservatives would be on a more solid foundation advocating for a simplified tax code whose purpose is to raise revenue, not to influence behavior.[39]

At least among otherwise conservative economists, the argument is that the carbon tax should capture the costs of externalities. Considering that the field of climate science is far from settled, the external costs of GHGs, if any, are very unclear, and the tax rate may need to change. Such uncertainty will undoubtedly hamper investment in carbon resources even more, with considerable uncertainty and the prospect that policymakers will make "polluters" (what liberals call those who develop and use fossil fuel resources) pay and reduce other taxes or spend increased revenues.[40] Such uncertainty and the likelihood of future gaming of the system would make it difficult to exploit our world-leading fossil fuel resources.

Another problem with a carbon tax is that it very well could be hidden. When he was an academic, Gilbert Metcalf, an economist who has served as Deputy Assistant Secretary for Environment and Energy in the Office of International Affairs at the U.S. Department of the Treasury,[41] co-authored a blueprint for taxing GHG emissions that was published in the *Harvard Environmental Law Review*. The paper states that:

> With respect to the tax base, we show that collecting the tax upstream would make it possible to accurately and cheaply cover 80% of U.S. emissions by collecting the tax at fewer than 3000 points, and that it would be possible to cover close to 90% of U.S. emissions at a modest additional cost.[42]

Clearly, such a tax is not meant to be collected at gas pumps or from utility customers, which would dramatically increase administrative costs. While a carbon tax could be more or less apparent to American citizens, depending on its design, the advocates of such a tax have no incentive to keep the tax small. In the words of Professor Thomas Sowell, "In general, the less visible a tax is, the more revenue can be collected without resistance or electoral retribution by the voters."[43] Accordingly, a major concern would be the visibility of such a tax.

A new carbon tax would simply give Washington another tool with which to stealthily raise revenues and manipulate American families' behavior, and any such tax should be rejected.

36. Curtis S. Dubay, "Obama FY 2013 Budget Violates Basic Principles of Tax Reform," Heritage Foundation *Backgrounder* No. 2665, March 19, 2012, http://www.heritage.org/research/reports/2012/03/obama-fy-2013-budget-violates-basic-principles-of-tax-reform.
37. *National Federation of Independent Business v. Sebelius*, 567 U.S. ___ (2012).
38. "Sugar-sweetened beverages" were one potential pay-for considered by the Senate Finance Committee for the health care reform law. "Financing Comprehensive Health Care Reform: Proposed Health System Savings and Revenue Options," Committee on Finance, U.S. Senate, May 20, 2009, p. 35, http://www.apapracticecentral.org/advocacy/reform/finance-may20.pdf.
39. Admittedly, using the tax code as the only form of regulation of pollution and emission of GHGs would be more efficient and would allow greater liberty than command-and-control regulation. "Pigovian" taxes are efficient in theory but seem to be much more difficult to make work in practice.
40. Washington's history in using new revenue streams for deficit reduction is not encouraging.
41. See "Five Questions with Gilbert Metcalf," August 24, 2011, http://www.treasury.gov/connect/blog/Pages/Five-Questions-with-Gilbert-Metcalf.aspx (accessed July 24, 2012).
42. Gilbert E. Metcalf and David Weisbach, "The Design of a Carbon Tax," *Harvard Environmental Law Review*, Vol. 33 (2009), http://www.law.harvard.edu/students/orgs/elr/vol33_2/Metcalf%20Weisbach.pdf (accessed July 17, 2012).
43. Thomas Sowell, *Basic Economics: A Common Sense Guide to the Economy* (New York: Basic Books, 2007), p. 458.

Poor Americans Hit Hardest

The poor tend to spend a higher proportion of their earnings on energy, particularly utilities and transportation. Moreover, some Americans use more fossil-fuel energy than others because of driving distances (rural families drive more—27,700 miles per household vs. 17,600 miles for urban households[44]); geography (less temperate weather means more heating and cooling costs); and already constructed energy infrastructure (coal plants are prevalent in the Midwest near mining operations). A carbon tax would disproportionately hit these families, whose behavior is difficult to change in the short run.

While economists like to imagine that the carbon tax would be offset by reductions in taxes on capital or some other particularly economically damaging tax, the fact is that, politically, it is far more likely that funding from the carbon tax would be used to reduce the tax's impact on the poor. Senator Barbara Boxer (D–CA), who chairs the Senate Committee on Environment and Public Works, rejected the idea of using new revenue from the carbon tax to reduce corporate taxes—a favorite idea among some on the center-right—and said that any revenues should be used "to make sure ... the middle class gets the breaks in the interim while we move to clean energy."[45]

AN ENERGY TAX WOULD HARM FAMILIES AGAIN AND AGAIN, BOTH DIRECTLY THROUGH ENERGY PRICES AND INDIRECTLY THROUGH HIGHER PRICES FOR GOODS AND SERVICES.

Nearly all of the cap-and-trade proposals introduced during the 111th Congress included measures to blunt the impact on less affluent families, but while such proposals would soften the blow for low-income households, an energy tax would harm families again and again, both directly through energy prices and indirectly through higher prices for goods and services.[46] As Congressional Budget Office Director Douglas Elmendorf has said:

> [A]t any point in which we are putting a price on carbon emissions, that would be passed through to the cost that consumers face on energy products but also all other products that are made using fossil fuels.... I don't know if there are any goods that use no energy in their production. It seems to me unlikely.[47]

Dampening the impact on poor families was deemed a politically necessary design element for cap-and-trade and would likely be required in any carbon tax. Looking at compliance costs for cap-and-trade (with an allowance price around $20 per ton), the Congressional Budget Office found that the lowest quintile lost more than three times as much income (measured as a percentage) as the top quintile (2.5 percent as opposed to 0.7 percent).[48] Because the poor spend a higher portion of their income on energy and the higher energy prices are passed on to the consumer,[49] this result is not surprising.

In fact, increasing consumer costs is a primary reason *for* pricing carbon, according to many of its proponents. As Treasury Secretary Timothy Geithner has explained, it is necessary for the price of energy to increase if "you're going to change how people use energy."[50] And who will change their behavior? It is far more likely that the poor and middle class—those who have to live from paycheck to paycheck and spend a bigger portion of their earnings on energy—will be forced to alter their lifestyles much more (drive less, heat and cool the home less, buy fewer goods and services) than the wealthy.

44. Oak Ridge National Laboratory, Center for Transportation Analysis, *Transportation Energy Data Book*, June 2011, Table 8.7, http://info.ornl.gov/sites/publications/files/Pub31202.pdf (accessed August 13, 2012).
45. Senator Barbara Boxer (D–CA), as quoted in "Boxer Hints Carbon Tax Could Be Part of a Larger Budget Deal," *Energy & Environment News PM*, July 31, 2012.
46. Kevin A. Hassett, Aparna Mathur, and Gilbert E. Metcalf, "The Incidence of a U.S. Carbon Tax," American Enterprise Institute *Working Paper* No. 21, January 31, 2008, http://www.aei.org/paper/energy-and-the-environment/the-incidence-of-a-us-carbon-tax/ (accessed July 30, 2012).
47. Douglas Elmendorf, testimony before the Committee on Ways and Means, U.S. House of Representatives, March 26, 2009, http://republicans.waysandmeans.house.gov/News/DocumentSingle.aspx?DocumentID=116686 (accessed August 15, 2012).
48. Congressional Budget Office, "The Economic Effects of Legislation to Reduce Greenhouse-Gas Emissions, Publication No. 4001, September 2009, http://www.cbo.gov/sites/default/files/cbofiles/ftpdocs/105xx/doc10573/09-17-greenhouse-gas.pdf (accessed August 9, 2012).
49. See, e.g., Robert Shackleton, "The Costs of Reducing Greenhouse-Gas Emissions," Congressional Budget Office *Economic and Budget Issue Brief*, November 23, 2009, p. 2, http://www.cbo.gov/sites/default/files/cbofiles/ftpdocs/104xx/doc10458/11-23-greenhousegasemissions_brief.pdf (accessed July 27, 2012).
50. Timothy Geithner, testimony before the Committee on Finance, U.S. Senate, March 4, 2009, www.c-span.org/Events/Treasury-sec-Geithner-at-Senate-Finance-Cmte/13037, 2:43–2:44 (accessed August 15, 2012).

In addition to a clamor that carbon tax revenue be used to counteract the tax's regressive nature, environmental groups and the alternative energy lobby will likely advocate that the revenue be spent to promote new, unproven "green" technology. So-called green energy companies that have started in response to a massive government infusion of capital into such enterprises ($44.3 billion in 2009 alone)[51] are failing, and some are calling for an increase in funding, which has been reduced to "only" $16.1 billion in 2012.[52] The carbon tax presents a tempting revenue stream for those companies and groups:

> A small portion of the funds might be directed to providing transition relief for displaced workers (such as miners), supporting basic energy research and development, solving vexing issues associated with bringing CCS to scale, constructing any necessary transmission lines, and perhaps encouraging conservation activities that market imperfections might otherwise block.[53]

Left unsaid is the overhead cost to administer the tax—these interests receive their money only after it has been cycled through Washington, D.C. A new carbon tax would seek to manipulate our behavior and would harm poor and middle-class Americans. For these reasons, it should be rejected.

Conclusion

Even if one concludes that carbon dioxide and other greenhouse gases are leading to increased temperatures—and there is robust debate and far from a public consensus on the magnitude of man-made warming, particularly among conservatives—a carbon tax would be counterproductive because it would do next to nothing to lower global temperature, while it would harm American manufacturing competitiveness, create a new revenue stream based on behavior modification, and harm low-income Americans.

Free-market conservatives in particular should denounce a new carbon tax as more meddling by the federal government. Specifically, they should urge Congress and the President to:

- Categorically reject a new carbon tax, which would have little environmental impact, harm manufacturing, be another tax seeking to control behavior, and disproportionately harm the poor;
- Work to stop EPA regulations of greenhouse gases, which will wreak havoc on the economy and have no appreciable impact on the stated environmental goal of reducing global GHGs; and
- Work toward tax reform that results in a system that will raise the revenue to fund necessary government operations in ways that cause the least possible economic damage and not pick winners and losers with preferential or punitive policies.

A carbon tax is in essence a perpetuation of a disastrous policy of picking winners and losers from Washington instead of allowing families to choose which energy sources work best for them. From ethanol subsidies to grants awarded to now-defunct solar manufacturers like Solyndra, these policies have increased costs to American families and wasted taxpayer dollars.

Energy, like other sectors, should not become a playground for connected lobbyists to collude with government for special treatment. The bottom line in energy is that supplies can be delivered and new supplies created through the private sector rather than through mandates, regulations, taxes, and subsidies ordered by government.

*—**Derrick Morgan** is Vice President for Domestic and Economic Policy at The Heritage Foundation.*

51. Jesse Jenkins, Mark Muro, Ted Nordhaus, Michael Shellenberger, Letha Tawney, and Alex Trembath, "Beyond Boom & Bust: Putting Clean Tech on a Path to Subsidy Independence," Brookings Institution, April 2012, p. 4, http://www.brookings.edu/~/media/Research/Files/Papers/2012/4/18%20clean%20investments%20muro/0418_clean_investments_final%20paper_PDF.PDF (accessed August 9, 2012).
52. Ibid.
53. Metcalf and Weisbach, "The Design of a Carbon Tax," p. 516.