

PERSPECTIVES ON BC'S CARBON TAX

BC Carbon Tax: Just Right?¹

Clark Williams-Derry[©]

BC energy guru Mark Jaccard argues in *The Tye* that the province's new carbon tax hits a sweet spot. Not too hard, not too soft, but just right. Apparently, the tax has been attacked from both the left (doesn't do enough to curb emissions, too hard on consumers) and from the right (hurts businesses, so high that it'll spur runaway inflation).

The fact that it's taking heat from both sides means nothing, of course. Sometimes, the critiques from one side or the other are simply wrong -- so policy-makers simply can't gauge whether they've achieved a balanced policy based solely on the tally of hate mail that lands in their inbox. But in this case, Jaccard makes some pretty compelling arguments that BC's recently announced carbon tax is just about as good as it gets in a democracy: not too fast, yet far-sighted enough to prompt genuine emissions reductions over the long term; effective, without creating the sort of economic disruptions that stir political opposition; and perhaps most importantly, more fair to low-income folks than the carbon taxes that have been levied in Scandinavia and the UK.

More on BC's Carbon Tax Shift²

Alan Durning[©]

On February 19, we applauded British Columbia's new carbon tax shift. I've now had time to digest the plan. It's even better than we said, and the province could tweak it to make it better still.

This policy is the purest instance of a tax shift that I've ever seen. It's an exceptionally faithful implementation of tax shifting—a policy innovation Sightline has been promoting since 1994 and especially since our 1998 book.³ (A small brag: Gordon Campbell read the book that year and told me he was going to shift taxes in his second term as premier. I didn't hold my breath, but now he has delivered.) The carbon tax shift (as opposed to the larger government budget it's wrapped in) is almost entirely untarnished by handouts to special interests. It is built on four principles:

- (1) **Revenue neutrality--shifting taxes from "goods" to "bads."** As the BC Finance Minister's plan says, *"All revenue generated by the carbon tax will be returned to individuals and businesses through reductions in other taxes. None of the carbon tax revenue will be used for expenditure programs."* That's good news for the province's

¹ Sightline Daily, Sightline Institute, 03/07/2008

² Sightline Daily, Sightline Institute, 03/10/2008

³ Durning, A.T. and Y. Bauman. 1998. *Tax Shift: How to Help the Economy, Improve the Environment, and Get the Tax Man off Our Backs*. Sightline Institute

economic vitality: tax shifting boosts opportunity, strengthens enterprise, and generates wins for families, prosperity, and our natural legacy.

- (2) **Phased implementation--an economy-friendly time line.** Carbon taxes rise from \$10 per metric ton of carbon dioxide equivalent (CO_{2e}) this year to \$15 next year, then \$20 the following year, and so on up to \$30 per ton in 2012. Personal and corporate income taxes decline on a similar schedule. A future government will decide whether to continue the dollar-for-dollar shift from income taxes to carbon taxes. This phasing is good news, because it lets families and businesses upgrade their appliances and machinery gradually, seizing opportunities for efficiency and innovation at the right times in the turnover cycle. Predictable tax increases spur us toward a smarter energy economy, while still giving us time to adapt gracefully.
- (3) **Tax benefits--Protection for working families.** “The bottom two personal income tax rates will be reduced for all British Columbians resulting in a tax cut of 2 per cent in 2008 and 5 per cent in 2009 on the first \$70,000 in earnings – with further reductions expected in 2010.” This income tax reduction will benefit everyone who pays income taxes, but it will benefit working families the most. In addition, low-income families will get an annual (and escalating) Climate Action Dividend; this year, it will be worth \$100 per adult and \$30 per child. Just like Cap and Buffer! The tax rate reduction plus the dividend give double protection to working families, which will help to compensate for the unfairness of climate disruption.

Working families may get side benefits from carbon taxation, too. For example, walking, cycling, and public transit all function better when more people are involved. More walkers and cyclists lead to safer streets; more transit riders support more frequent service. Todd Litman of the Victoria Transport Policy Institute points out that more parents seeking carpools make carpooling easier for all; more parents walking their kids to school make “walking school buses” easier to organize. So if carbon taxes shunt more middle-class people toward these low-cost, low-carbon alternatives, working class people may benefit.

- (4) **The broadest possible coverage.** The carbon tax falls on all greenhouse-gases emitted from the burning of fossil fuels within the province: gasoline, diesel, natural gas, coal, heavy fuel oil, propane, kerosene—you name it. It’s exceptionally comprehensive. That’s good news, because it will make the tax credible, defensible, and efficient to administer. Most countries with carbon taxes, including tax-shifting’s pioneers in Scandinavia, have made one political compromise after another, exempting whole industries and fuels and thereby undermining the effectiveness and logic of the tax. British Columbia’s policy is a model.

It doesn’t yet include emissions from industrial processes, such as cement manufacturing and aluminum smelting or from “fugitive” sources, such as leaks of methane from pipelines and landfills. But those things are hard to measure, and the province’s plan states the government’s intention to include them too in time. Similarly, it excludes nonfossil carbon that comes from the atmosphere and ends up in wood, other biomass, and biofuels. (Biofuels’ climate impacts look worrisome, of late, but the province’s policy is logically consistent.) It also exempts exported fuels—including those in the fuel tanks of ships and airplanes that travel to other jurisdictions—because these fuels are not burned inside the province. When it comes time to integrate BC’s carbon tax with future ones in neighboring jurisdictions, or with cap and trade systems, its purity and consistency will be a huge advantage.

Not that BC's smart tax shift policy can't be even better. It can. Some critics in British Columbia are disappointed in the tax shift for its modest starting rate of just \$10 per ton (which works out to about 9 cents per gallon of gas). Tax shifting, however, is supposed to start small, so I like where it starts, particularly because no nearby jurisdictions yet have carbon pricing at all. My disappointment is where the tax shift ends. It only continues until 2012. Although it's courteous of Premier Gordon Campbell not to commit his successors to ongoing rate increases, only such continuing rate increases will deliver on the tax shift's promise. To avert the rank unfairness of climate disruption, the price of carbon ultimately needs to rise substantially. If BC extends its plan for twelve yearly increments--not just the five increments outlined last week--the province's carbon tax rate will still be lower than the existing rate in Sweden (\$69/metric ton of CO₂). And Sweden's rate clearly isn't high enough yet to engender a clean-energy revolution.

This observation isn't just a matter of future influence; it's about the present. In fact, advance notice of future carbon price increases are as important as the increases themselves. If British Columbians know that the price of fossil fuels is going to go up every single year for as far into the future as the eye can see, they'll make different decisions now. They'll choose different jobs; live in different neighborhoods; and buy different homes, cars, and appliances. Businesses, too, will expand their thinking to fit a new energy era: they'll invent different products, market different services, deploy different technologies, and develop different business strategies. Again, the influence of a tax shift isn't just that carbon prices will be higher; it's that they're sure to keep rising. Psychologically, that's a huge difference.

Still, I don't want to criticize much, especially considering the still-skeptical reaction of many British Columbians. Even without extension into the future, BC's carbon tax shift is a huge political breakthrough. It's revenue-neutral, phased, comprehensive, and equitable. It's ready to be copied elsewhere in Cascadia and beyond. And I mean that literally: copied and pasted into the law books. It's that good.

BC Carbon Tax Shift: Not as Good as it Used To Be?⁴

Clark Williams-Derry[©]

BC's landmark tax shift is falling more heavily on the poor.

We've been rather outspoken in our support of BC's carbon tax shift. It stands out among global carbon pricing policies as particularly well-designed, for at least two reasons. First, it's comprehensive and consistent. Most other policies around the world that put a price on carbon emissions also contain exemptions or loopholes that miss large parts of the economy, or apply different kinds of rules to different fossil fuel users. But BC's carbon tax shift applies evenly to all CO₂ emissions from fossil fuels, so it creates consistent, uniform, and economically efficient pressure to reduce climate-warming emissions. Second, BC's tax shift, at least as it was originally structured, contained built-in economic protections for lower-income families that stand to lose the most from higher energy prices. That's key, since a poorly-designed carbon pricing policy has the potential to fall heaviest on poor folks--the people who've done the least

⁴ Sightline Daily, Sightline Institute, 07/12/2010

over time to generate climate-warming emissions and who have most to lose from global climate disruption.

But Marc Lee of the Canadian Center For Policy Alternatives-BC, who's also generally a supporter of the carbon tax shift, is increasingly wary of the policy's impact on the province's lower-income folks. When it was introduced back in 2008, the carbon tax dedicated about one-third of revenues to a low-income credit . . . This was a big positive with households in the bottom 40% of the distribution slightly better off on average, with credits exceeding taxes paid. Alas, last year's increase to \$15 a tonne wiped out that gain because the low income credit barely increase in value (from \$100 per adult to \$105), while the carbon tax grew by 50%.

The new 2010 increment to the carbon tax will make the whole regime regressive – meaning a bigger hit to low-income families relative to their income; they will be absolutely worse off even after considering the credits. Drat. The lesson here, perhaps, is that good things can come to an end: it takes vigilance and political pressure to keep even the best-designed of policies from morphing into a form that's not nearly so benign.

BC'S Carbon Tax Turns Two^{5,6}

Marc Lee[©]

With all of the attention focused on the HST implementation on July 1, most people seemed to miss the next increment of that other much-hated tax, BC's carbon tax. As of July 1, the carbon tax is now \$20 per tonne of CO₂, or about 4.6 cents on a litre of gasoline. And like any two-year old, this toddling tax increase is set to wreak some havoc on the household.

What the carbon tax shares with the HST is a bigger hit to the bottom of the income distribution. When it was introduced back in 2008, the carbon tax dedicated about one-third of revenues to a low-income credit (the remainder going to personal and corporate income tax cuts). This was a big positive with households in the bottom 40% of the distribution slightly better off on average, with credits exceeding taxes paid. Alas, last year's increase to \$15 a tonne wiped out that gain because the low income credit barely increase in value (from \$100 per adult to \$105), while the carbon tax grew by 50%.

The new 2010 increment to the carbon tax will make the whole regime regressive – meaning a bigger hit to low-income families relative to their income; they will be absolutely worse off even after considering the credits. For the bottom 40%, the numbers are not huge – about a \$30 per year loss, but pile that on top of the HST and you get the picture. That said, it could have been worse: the 2010 budget increased the credit another ten bucks to \$115.50 per adult.

One might argue that the whole point is to get all households to change their behaviour in response to the carbon tax. But it is the lowest income families that have the hardest time making the capital investments needed to get ahead of the curve, and who are most locked into carbon necessities (such as heat) that are difficult to reduce easily. High income families have a much easier time reducing their consumption and upgrading their homes for energy efficiency.

⁵ Canadian Centre for Policy Alternatives – BC Office Updates, July 5th, 2010

⁶ Note: Figures cited are based on my 2008 report with Toby Sanger, *Is BC's Carbon Tax Fair?* Numbers have been updated based on information in Budget 2010.

Like the HST, the carbon tax brings a windfall to business, with a large chunk of this year's revenue going to corporate income tax cuts. Back in 2008, the projected recycling to business tax cuts in 2010/11 was estimated at \$333 million. In the 2010/11 budget that amount has been souped up to \$412 million – more than half of the anticipated \$796 million in carbon tax revenues – to add onto savings coming from the HST.

Since all taxes are ultimately attributable to households, corporate tax cuts are essentially upper income tax cuts. On this basis, the top 20% of households (who own the vast majority of shares in businesses) are actually huge beneficiaries of the carbon tax regime. Not counting the corporate tax cuts, the top 20% of households would pay about \$536 more on average in carbon taxes than they receive in personal income tax cuts, but if we include the corporate tax cuts they receive a net benefit (tax cuts less carbon taxes) of \$291.

The remaining carbon tax revenues are recycled into personal income tax cuts. In 2008, this was supposed to be \$410 million in personal income tax cuts. By the 2010/11 budget that number had been almost halved to \$211 million (there is also \$20 million in benefits to northern and rural households in addition to this).

Don't get me wrong: carbon taxes are still an important policy tool in battle against global warming. In fact, at \$20 per tonne we are only now just getting into the range of carbon prices that will start to change behaviour. Currently scheduled increases go to \$30 per tonne in July 2012, but after that we do not know where the BC government will go with the tax. A study for the David Suzuki Foundation and Pembina Institute by Mark Jaccard and Associates concluded that carbon taxes needed to hit \$200 per tonne by 2020 if we are going to achieve our GHG emission reduction targets.

That's a steep price increase, and that is why we need to get the details right around how the proceeds of the tax are redistributed. Given the need of lower-income households to adapt, there is a compelling case to be made to significantly increase the share of revenues going to a refundable credit – like half of the carbon tax revenues, with more households in the middle-income range benefitting as well. (In fact, pooling the carbon tax credit with the HST/GST credits into a consolidated credit and greatly increasing their values would be a nice step towards a guaranteed income, but I digress.)

The other half of carbon tax revenues should not go into further personal and corporate income tax cuts, and instead should be used for major improvements in public transit, energy efficiency retrofits, and green jobs training programs. In 2010/11, the carbon tax is estimated to bring in almost \$800 million in revenue, rising to \$1 billion next year. That is some serious cash that would greatly accelerate climate action in BC.

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