



*Ayres Law Group*

## Air & Energy Policy Alert

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### ***Could a Carbon Tax Become Part of a Bipartisan Debt Reduction Strategy?***

Now that the government is facing an early-August deadline for increasing the federal debt limit, Congress and the President are searching for ways to reduce the federal debt. There are hints that a carbon, or more accurately, greenhouse gas (GHG), tax could be a way to raise revenue for the federal government. Though the odds are long, circumstances could combine to create bipartisan support for a GHG tax as part of a “grand bargain” to solve the debt reduction conundrum.

This conclusion emerges from a series of studies recently funded by the Peter G. Peterson Foundation, an organization dedicated to creating public discourse about ways to address the country’s fiscal challenges. Six organizations of widely different political views drafted plans to reduce the nation’s debt. Four of these — the Center for American Progress (CAP), the Bipartisan Policy Institute, the Economic Policy Institute (EPI), and the American Enterprise Institute (AEI) — included proposals to institute a price on carbon in their plans, suggesting that a tax could become a politically viable means of raising a substantial amount of revenue. Notably, support of the right-leaning AEI for the concept may signal that conservatives in Congress who have rejected any increase in income taxes might be willing to consider imposing a tax on carbon as part of an overall debt limit deal.

### ***Revenue Generation***

A tax on GHG emissions could raise \$99 billion in revenue in just one year (taking 2009 as a sample year, taxing the total GHG emissions in the U.S. (6.6 billion metric tons of CO<sub>2</sub> equivalent) at a rate of \$15 per ton of GHG emissions). The potential to raise this amount of revenue made a GHG tax attractive to the four organizations, above.



### **Program Proposals**

- Center for American Progress. CAP proposed instituting a carbon price to achieve reductions in GHG emissions similar to the Waxman-Markey cap-and-trade bill, which passed the House in 2009 (42% from 2005 levels by 2030 and 83% by 2050).
- Economic Policy Institute. EPI recommended distributing half of the proceeds from a carbon tax to consumers to compensate them for rising energy costs. The other half of the revenue would be used for deficit reduction and “green investment.” EPI said its proposed carbon price (~\$16 per ton CO<sub>2</sub>e) could generate \$52 billion dollars to be used for deficit reduction by 2015.
- American Enterprise Institute. AEI would abolish subsidies for alternative fuels and energy tax credits, and regulations intended to reduce GHG emissions. Instead, the group recommended imposing a carbon tax in 2013 that would phase in so that in 2017 the tax would be about \$26 per ton of GHG emissions. Each year until 2051, the tax would increase 5.6 percent over the previous year’s tax.
- Bipartisan Policy Institute. BPI examined a revenue-generating option that would set a price of \$23 per ton of CO<sub>2</sub> emissions in 2018 and rise 5.8 percent each year thereafter. The group found that of the alternative sources of revenue it considered, the carbon tax received the greatest amount of support.

### **Outlook**

Given the political diversity of these organizations, it may be possible that there could be bipartisan support for a carbon tax. Democrats have argued that increased revenue must be a part of any deficit-reduction legislation, while Republicans have been equally adamant that there be no increases in income tax. A tax on carbon, if paired with significant spending reductions, might be an acceptable means of meeting both imperatives.

Republicans could argue that they are moving away from taxing “goods,” like people’s income, and towards taxing “bads,” like pollution. Democrats who support reductions in GHG emissions could point to the tax as addressing the serious problem of global warming. Also, a carbon tax would be mildly progressive, since the carbon intensity of people’s lives tends to correlate with wealth.

With the debt limit deadline looming, Congress and the White House will be forced to take action by early August to avoid defaulting on federal debts. A carbon tax is probably politically viable only under the pressure-cooker conditions that will prevail in July. Given leadership from the White House,



just enough bipartisan support might be generated to include a GHG tax in the debt reduction legislation. In the House, a package including a carbon tax might be more acceptable than repealing some of the Bush income tax cuts for the higher income brackets.

As stand-alone legislation, any serious GHG tax proposal would inevitably endure the same horse-trading that took place in the cap and trade debate. For example, taxed industries would no doubt prefer some of the proceeds be distributed back to them in the form of transition assistance, especially those industries which do not appear to have a short-term low-carbon alternative, such as coal-fired power plants. But if a tax were included in a debt limit bill, the same interests that fought hard against climate legislation in the past may not have time enough time to mobilize to combat the tax, and might have to seek amendments *after* a carbon tax is enacted, when they will be more difficult to obtain.

Without question, a carbon tax is a long shot, even in debt limit legislation. The chances of enacting such a tax depend heavily on President Obama's leadership. His budget, however, already includes revenue from a greenhouse gas control program. Perhaps this is the tool he may choose to fill that line item.

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