

Pollution tax rebates little help for low-income workers

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Although policymakers believe the regressiveness of pollution taxes can be offset by returning revenue to the low paid through a reduced labor tax, that approach may not work, and also could have the unintended consequence of shrinking some workers' overall real net wages, according to research by a University of Illinois energy policy expert.

Don Fullerton, a finance professor and former deputy assistant secretary of the U.S. Treasury Department, says that using revenue from pollution taxes to lessen its regressiveness on low-wage workers is not enough to offset higher commodity prices and shrunken real wages that would result from such a tax.

"Revenue from a carbon tax would certainly help, but it wouldn't be enough to protect low-wage households from any harm," said Fullerton, a researcher in the U. of I. Institute of Government and Public Affairs and the Center for Business and Public Policy in the College of Business. "A carbon tax is going to have costs, and while we might be able to play with the distributional burden of the costs, it's hard to protect low-income workers completely. There may just not be enough money to help them out."

Any sort of carbon tax, cap-and-trade or carbon pricing is likely to raise the price of commodities consumed by low-income people – an undesirable effect that lawmakers are aware of, Fullerton said.

Although the cap-and-trade bill that passed the House is now dead,

lawmakers wrote the bill with an eye toward helping low-income [households](#) purchase electricity.

"I think policymakers in general recognize that it's going to have regressive effects when the prices of electricity, gasoline and heating fuel go up, because these goods make up a big fraction of low-income budgets," said Fullerton, an expert on the economic impact of environmental regulations. "That's why these types of tax rebate proposals are floated, to make a pollution tax or a carbon tax more politically viable."

According to the research, even though the pollution tax injures both high- and low-skilled labor through higher prices of goods and services, the wage rates for low-skilled labor also declines. In almost all of the study's economic models, the rebate of all revenue to low-skilled labor still does not prevent a reduction in their overall real net [wages](#).

"If a firm is going to reduce its carbon emissions, it might do more of something else," Fullerton said. "In order to cut emissions, they might need more high-tech abatement capital and labor, and that means buying more high-skill labor. That drives up the high-skill wage, which is going to help high-wage earners but hurt lower income people through another mechanism. So the effects of pollution taxes are felt not only on the 'uses' side of income in the form of higher product prices, but also on the 'sources' side of income with declining relative wage rates for low skilled workers."

But just because the poor would bear a burden of a [carbon tax](#) doesn't mean it's not worth doing in some form or another, said Fullerton, who heads the environmental and energy economics program for the National Bureau of Economic Research, a nonprofit, nonpartisan think tank that provides economic analysis for government, business and the academic community.

"The take-home message is that there's no such thing as a free lunch," he said. "Everyone is going to bear some costs of carbon pricing, but the point of it is to avoid the even greater costs of global warming and climate change.

"Nobody wants to bear these costs, but the alternatives are much worse – more carbon dioxide and greenhouse gases, more climate change, global warming, and more extreme weather events. All of these bad outcomes disproportionately hurt the poor."

More information: The paper is "Can Pollution Tax Rebates Protect Low-Income Families? The Effects of Relative Wage Rates".

Provided by University of Illinois at Urbana-Champaign

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