

[Not quite as bad as I'd thought](#) [1]

Written by [Tim Worstall](#) [2] | Monday 4 August 2008



The Sunday Times [tells us](#) [3] that these calls for a windfall tax on the energy companies aren't being listened to in the way [I'd been worried](#) [4] they could be. Rather than hammering the profits being made they're rather thinking about:

The government has already announced proposals to raise £2 billion over four years by auctioning so-called "emissions permits". Previously these permits, created under the European Union's carbon trading scheme, were free. Ministers are examining ways of raising more cash from the auctions. If the proportion of permits auctioned for money is increased from the existing 7% to 10% the maximum allowed under EU rules a further £500m could be raised from power companies in the coming 12 months.

That's certainly more sensible. There's two things that we need to understand about these permits and green taxes. The first is that there's a difference in the effects of a carbon tax and these cap and trade systems using permits. With tax we know what the cost will be, but not what the emissions reductions will be. With permits we know what the emissions will be but not the cost. I prefer the tax because it makes clearer and more transparent the cost benefit analysis: but feel free to differ. But if the tax and the permit prices turn out to be at the same level then the two systems are functionally equivalent.

However, a cap and trade system where some permits are given away is not the same as a carbon tax. It's the same as a carbon tax plus corporate pork. Those lucky companies that get given permits make unearned profits from them. Even if every extant company gets the same proportion of freebies, that still leaves potential new competitors at a disadvantage, they will have to buy all of their permits on the market. It's protecting the incumbents again.

So that's our first lesson about green taxes: if we're to have a cap and trade system of permits then all permits need to be auctioned, not just that 10% limit.

The second is that moving the tax system from taxing "goods" to taxing "bads" doesn't actually mean that we want to raise the general level of taxation. It doesn't mean that when we tax carbon (or sell permits) to reduce emissions that we thereby hand another pot of money to the politicians for them to waste. No, far from it, what we actually need to happen is that other taxes elsewhere in the economy get lowered by the amount raised. As, amazingly, was done with the Landfill Tax: the amount raised would be compensated for by reducing that worst of taxes, employers' national insurance (changed to reduced corporation tax in 2007).

If auctioning 3% of permits would raise £500 million, then auctioning the other 90% might raise £15 billion.

There's about 30 million tax payers, so that could be used to raise the personal allowance by £2,500 each (basic rate is 20%, so 30 million x £2,500 x 20% = £15 billion will be the revenue lost from this move), getting us that much closer to our goal of taking the poor out of income tax altogether. Very rough numbers, I know, but increasing taxes on those bads must be balanced by reducing them on the good things.

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