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# Editorial

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## Taxation and the environment

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The European Commission has proposed a Community-wide 'carbon tax' as a means of reducing noxious emissions and thus controlling environmental pollution. At least, that was the starting point. But in order to deny an unwarranted competitive advantage to the French, with their exceptional investment in nuclear power, the tax would be extended from coal and oil to all fuels. And in order to maintain the international competitiveness of Community firms, the heaviest users of energy (including the heaviest users of coal) would be exempt from the tax.

So far the logical confusion is merely two-dimensional: the inclusion of nuclear power (to which a different set of considerations applies) and the exclusion of heavy users (who would be the principal targets of a tax intended to reduce pollution). But there is worse to come. The proposed tax would be imposed on the present widely varied pattern of fuel taxes and subsidies (notably explicit or implicit subsidies to nationalised concerns); and the question has still not been asked, let alone answered, whether taxation is the best or an appropriate means of controlling environmental pollution or whether other means of government intervention should be preferred. The central question is not how environmental taxes should be levied but whether they should be levied at all.

The idea of environmental taxation based on the principle that the polluter should pay goes back at least to Pigou's 'The Economics of Welfare' in the 1930s. The government was to intervene to correct 'market imperfections', and tax was a prime instrument of intervention.

The appeal of this argument to common sense is such that its hold on the public has largely withstood refutation at the academic level going back for some thirty years. One dimension of this refutation is the analysis of the public choice school (Nobel Prizewinner Buchanan and others) showing the falsity of the contrast between perfect government and imperfect markets: markets may be imperfect, but in all relevant respects government may be no less so. The second dimension derives from the work of Ronald Coase ('The problem of social cost', *Chicago Journal of Law and Economics*, 1960) showing that the principle 'the polluter pays', for all its appeal to distributive equity, is not superior in economic efficiency to the polluter's being bought off by the aggrieved party. For example, the concept of the developed countries' 'buying off' the destruction of rain forests in the Third World is a good illustration of Coase's argument.

Among those who have studied the subject seriously at academic level, there is no consensus that the polluter should pay. That principle competes not only with Coase's argument that the result is just as efficient if the 'injured party' pays but also with the assessment that making the polluter pay through the tax system may be less efficient than other means of control such as market-based regulation, articulation and extension and property rights, auctioning of planning permission, tradable licences to pollute, and so on. At the population level, there is the objection that the 'polluter pays' principle appears to license pollution providing that the polluter is rich enough to pay the relevant taxes or fines.

There is thus a risk that consideration of major questions (such as whether taxation can make a useful contribution to the control of environmental pollution and, if so, what) may be submerged in a welter of technical discussions about which form of tax is most suited to the purpose and that the best options may in consequence be ignored. The taxation of road space provides an instructive analogy. Significant proportions of the road network are congested in every Community country and it is tempting to argue that the price of petrol should be further raised through taxation in order to compel the public to economise on the use of roadspace. But (among other disadvantages) this would have perverse effects in rural areas where the road network is in oversupply and transport services in undersupply. The macroeconomic policy of raising the petrol price for everyone may well be inferior to the macroeconomic policy of charging for the use of road space on the same lines as the use of car parks is charged for already.

The fact that a policy might inflict serious losses on the Community or the world as a whole need not under present institutional arrangements constitute any obstacle to its proposal by the Commission or its acceptance by the Council of Ministers. If wiser counsels are to prevail, the taxpaying community will have to make its voice heard on the subject of the Commission's proposal for a carbon tax.