Pros and cons of carbon pricing: tax vs. market mechanisms

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African DNA Workshop
Marrakesh, 11 April 2015
Climate policy tools for emission reductions

- Command and control - mandated reductions
  - Technology standards
  - Performance standards
- Information/education/awareness
- Carbon pricing
Carbon pricing

• Carbon taxes and charges
  – Imposing a tax on either emissions or a proxy thereof

• Emissions trading: Cap-and-trade
  – Capping emissions and allowing compliance entities to trade between them allowances

• Offsetting (i.e. CDM) is not a carbon pricing mechanism!
The theory

Source: http://www.env-econ.net/carbon_tax_vs_capandtrade.html
Taxes vs. Emission trading

• Taxes:
  – administratively simpler?
  – easier to incorporate into existing tax codes and efforts
  – Revenue raising
  – Continuous incentive
  – Certainty of price incentive

• Emission trading
  – More in line with private sector performance
  – Certainty of environmental outcome (the cap)
  – Revenue raising
  – Continuous incentive
  – Possibility of offset development
  – Wider participation of different players (e.g. Traders, consultants, project developers)
  – International linking of markets and potential long term international price
Which is better: tax vs. Markets?

• Not an either/or discussion
  – Note that many European countries have both a carbon market (the EU ETS) and carbon taxes
  – Note also hybrid schemes such as RSA’s and Mexico’s
• No clear-cut argument for one or the other
• Choice depends on national conditions and circumstances
• Internationally, harmonization of taxes is close to impossible
• Taxes also do not usually allow for international cooperation
• The revenue raising argument for taxes is also not clear-cut
Thank you!

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