

Thoughts on carbon taxes

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I was asked my thoughts on carbon taxes yesterday. I prepared this rather quick note, which explains why I am unenamoured of them and think they have little part to play in a green transition which also seeks social justice and tax fairness:

- * **Carbon taxes exist to change behaviour**

- * They cannot do so by themselves

- * They need explanation

- * And in some (maybe a great many) cases regulation on carbon use may be more effective than carbon taxes

- * The argument made by the IMF and others, that carbon taxes as repricing, might be the best tool to bring about a change in carbon usage is not true

- * Regulation is better

- * And unless alternatives to the products subject to carbon taxes are available at the time that those taxes are introduced it is very likely that the result of introducing the tax will be profoundly negative outcomes that might harm the objectives of the tax

- * This means that before any carbon tax is considered a full appraisal of consequences is essential and investment in alternatives is essential

- * **Carbon taxes have to raise revenue or they will not work, but the consequences have to be appraised with care or the impact may be highly undesirable**

- * The problem with taxes is that their 'incidence' is not the same as the people who necessarily pay them. Incidence is on the end user who actually bears the cost.

- * In the vast majority of cases the incidence of carbon taxes is on consumption.

- * Those on lowest incomes in society have the highest marginal propensities to consume i.e. they spend a greater part of their income on consumption than anyone else. This means that almost all carbon taxes, however superficially constructed, will be

regressive in nature: there is almost no way round this.

- * What this means then is that any carbon tax has, then, to be balanced by deeply redistributive measures on other taxes to ensure that the price of saving the planet does not fall on those least able to bear it.
- * This, then, requires, the introduction of multiple tax measures that will increase liabilities owing for the most vociferous in society - the wealthier middle class. Whether this is possible is open to question. It must also be questioned how the payment to compensate those on lower income will be managed, what the take up will be, and whether the linkage will be understood. The risk of backlash is very high.
- * There is another issue: if the demand for the products that will carry the carbon tax is very inelastic - partly because of consumer preference and partly because of the lack of viable alternatives - then imposing a tax may only raise revenues and not change behaviour at all. All these issues have to be taken into account in considering any such taxes.

* **The result is that the range of viable carbon taxes, as such, is very small.**

* We already have airport taxes, and landfill taxes which are proxy carbon taxes. We tax hydrocarbons, significantly (but maybe not enough). We do not tax domestic energy, much.

* So what can we do?

* First, hit the really big targets:

* Aircraft fuel

* Bunker fuel

* This is possible: either in the UK or by imposing a tax on aircraft / ships landing if they have fuelled in low tax jurisdictions, but international cooperation would probably be required

* Effectively we impose a tax via variable landing fees dependent on tax on fuel already paid. These have the advantage of being capable of being ramped up quite easily over time.

* Then remove the subsidies for existing carbon usage e.g. investment reliefs for investment in these sectors. This may be one of the most useful things we could do.

* I personally believe in what I have called a CUT - a carbon usage tax that would be a financial transaction tax on flows through private bank accounts that would impose little or no charge on median earners (and maybe a bit above that) but which would be quite progressive and charge those with substantial flows to an additional tax that a) compensates for the lack of VAT that they pay b) is intended to redistribute income and

wealth and c) is not hypothecated for green purpose (because I oppose all hypothecation because you cannot fund a good from a bad, by definition, because if the bad ends then so too does the good and that might be undesirable) but is broadly indicated to be available for this purpose.

*** Thereafter I suggest regulation be primarily used on this issue. I simply don't see a role for carbon taxes in most cases.**

For those who prefer the mindmap version, this is it (click on it and then click again for a large version):