

# ENVIRONMENTAL TAXATION IN DEVELOPING COUNTRIES: SOME NOTES

Michael Keen \*

\*Tokyo College, University of Tokyo; CERDI; Centre for Business Taxation; IFS

*Global Development Network Conference on Tax Policy*  
November 3, 2022

# Preliminaries

Report for Ministry of Europe and Foreign Affairs, France, under the MRIP platform—to be launched in December

Overarching questions:

- If environmental taxation is such a great idea for developing countries, why don't we see more of it?
- In which areas—precisely—are there opportunities for good environmental tax policies?
- Are there risks of bad tax policies?

Some eclectic notes with these questions in mind:

## Some General Observations

- Taxation is not always the best way to address environmental problems...
  - e.g. regulation or tort law may be better...and is almost never enough on its own
- Environmental tax reform is often about reducing subsidies
- Climate change mitigation is not the most pressing environmental tax concern in most developing countries
  - Waste management, air quality, soil degradation, water supply, congestion...
- The key purposes of environmental taxation are environmental
  - Revenue potential is rarely transformative
- Subsidizing good things is different from taxing bad things—and generally worse

# Some points of principle and practice

## *Principle:*

- Point about Pigovian taxation is that with appropriate transfers ALL can gain
  - Compensation is inherent in the logic of corrective taxation, as well as likely wise politically and (perhaps) distributionally
- Environmental taxes (e.g. on energy) can worsen tax distortions
  - Corrective add on may be smaller the greater the need for revenue
  - But 'informality' can act in the opposite direction

## *Practice:*

- Potentially important role for local governments
- Administration and compliance matter: avoid nuisance taxes
- Tax policy also important in the guise of public sector pricing

## On carbon taxation

- Even leaving historical responsibility aside:
  - It is the large emitters that really matter for mitigation (US, EU, China, India..)
  - Strong equity—and even efficiency—case for lower climate-related carbon prices in low income countries
- But also, leaving climate aside, strong (second best) case for taxing fossil fuels to address local pollution:
  - air quality, accident externalities, congestion...
- Not the hardest taxes to administer
- Not necessarily regressive in developing countries
- Adverse impact on oil producing countries
  - with potential implications for fiscal regime design
- Coordination issues:
  - Border carbon adjustment: What impact on developing countries? How should they respond?
  - An international carbon price floor?

# Overcoming Resistance: Two Options

## *Cash compensation:*

- Dilutes revenue, but e.g. for fuel subsidies compensating lowest 2 deciles will leave much more than 80 percent of the revenue
- Increasingly feasible e.g. using biometrics
- But can reduce the efficiency gain

## *Earmarking:*

- More common for environmental than other taxes—in some cases as a form of compensation
- A strong case against:
  - If earmarking really limits spending, it over-constrains expenditure policy
  - If it does not, it is "An exercise in...misleading taxpayers rather than expanding democracy" (IFS, 1993)
- But...