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THE DIVIDEND ADVANTAGE

The 10 Reasons Why Rebating All Carbon Fee Revenues
Directly to the American People Offers the Most Popular,
Equitable and Politically Viable Climate Solution



by

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THE DIVIDEND ADVANTAGE

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ABOUT THE CLIMATE LEADERSHIP COUNCIL

The Climate Leadership Council is an international research and advocacy organization founded in collaboration with a who's who of business, opinion and environmental leaders to promote a carbon dividends framework as the most cost-effective, equitable and politically-viable climate solution.

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EXECUTIVE SUMMARY

There is widespread agreement among economists that a carbon fee offers the most cost-effective way to reduce greenhouse gas emissions. Top corporations and environmental groups, as well as opinion leaders from across the political spectrum, are increasingly converging around the idea. As support for a revenue-neutral carbon fee grows, however, there are diverging views about how to use the revenue.

Interest groups are lining up behind a variety of potential revenue uses, ranging from: cutting the deficit; reducing corporate or personal taxes; investing in green technologies and infrastructure; and financing climate adaptation and remediation.

In assessing possible revenue uses, it is critical to recognize that the primary obstacle to a carbon fee has long been political. The key to making a carbon fee popular and politically viable is finding a countervailing incentive that outweighs the fee's burden. The best candidate is carbon dividends, which would put money directly into people's hands.

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Simply put: all proceeds from a nation's carbon fee would be divided equally among its citizens and returned directly to them. Conferring financial benefits in the here and now would

fundamentally alter the cost-benefit time horizon of climate mitigation, re-casting a carbon fee as a popular and even populist solution.

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Carbon dividends also open the door to business and bipartisan support, which will require trading a robust carbon price for regulatory relief. Striking this “grand bargain” will hinge on both sides believing it will hold: environmentalists must be assured that the carbon fee rate will continually increase until emissions targets are met, while businesses and conservatives must be assured the corresponding regulatory simplification will last.

A major advantage of pairing carbon fees with dividends is that the latter's popularity would ensure the policy's longevity, giving environmentalists and businesses the confidence they need to strike a lasting political bargain.

Climate policy in the United States has been deadlocked for far too long, forestalling what economists of all stripes agree is the most cost-effective solution. The key to unlocking this puzzle is selecting the most popular, equitable and politically viable use of carbon fee proceeds.

1. MOST POPULAR

Public support for pricing carbon is highly dependent on how the revenue is used. By far the most popular use – by a ratio of 3 to 1 – is returning the proceeds directly to all citizens in the form of dividends.¹ The reason for this popular appeal is obvious: over two-thirds of American households would be financial winners under a carbon dividends plan. Recent polling reveals that a majority of Americans favor a carbon dividends plan, including support by a 3 to 1 margin among Republican voters.² Among 18-35-year-olds – the cohort that will determine the future of any party – support reaches 4 to 1. No other approach to carbon pricing comes close to this level of popular support.

The Alaska Permanent Fund Dividend illustrates the enduring popularity of dividends. Enacted in 1982 by a Republican Governor in a Republican state, it provides over \$1,000 per year to each state resident. This program has consistently proven popular across all income groups, turning it into a “third rail” that has withstood all efforts to tamper with it. The dividend is particularly popular among the 72% of Alaskans who make less than \$50,000 per year. But even Alaskans making more than \$100,000 per year prefer the dividend to income tax cuts.³ The durability and popularity of the Alaska dividend provides an important lesson for carbon fee advocates.

“The majority of Americans favor a carbon dividends plan, including support by a 3 to 1 margin among Republican voters and by a 4 to 1 margin among 18-35-year-olds

2. CARROTS TRUMP STICKS

The primary impediment to US climate progress may be the least recognized: a fundamental psychological barrier. The prevailing message espoused by climate advocates, at its core, is that we should make short-term sacrifices now for the benefit of other people, in other countries, thirty to forty years in the future. This runs contrary to what extensive psychological research confirms is our “loss aversion” preference: we place a higher value on avoiding short-term pain, even if it leads to greater long-term gain.^{4,5} Like it or not, human nature is inherently self-interested, and we will only solve our climate problem at the required scale and speed if we recognize this.

A winning climate strategy must offer the public a countervailing “carrot” that more than compensates them for the necessary “stick” of higher fossil fuel prices. The most politically viable way to do so is by rebating the proceeds from a carbon fee directly to all American citizens on an equal basis. And this carrot is quite significant: a family of four could receive approximately \$2,000 in dividends per year. The appeal of cash dividends offers a game changing “saliency” that is immediately tangible to ordinary citizens. This fundamentally alters the cost-benefit time horizon for climate action, while re-messaging a carbon fee around a far more compelling narrative.

3. MOST EQUITABLE

A common concern is that carbon fees can be regressive, imposing a disproportionate burden on the least fortunate. Combining carbon fees with dividends solves this problem and ensures that the most vulnerable come out ahead. The reason is simple: the wealthier tend to pollute more, and therefore would face higher costs. Importantly, however, these dividends are neither giveaways nor a new entitlement. Since costs increase in direct proportion to one's carbon footprint and all citizens receive identical dividends, everyone is rewarded equally for reducing their carbon footprint.

Numerous studies confirm the distributional advantages of dividends over all other uses of carbon fee proceeds.⁶ For example, the US Treasury found that 70% of American households would benefit, because on average they would receive more in dividend payments than they would pay in increased energy prices.⁷ And the bottom income deciles – those who have the most trouble making ends meet – would experience the greatest net gains. The dividend pathway is the only approach to carbon pricing that would result in higher median household incomes for the vast majority of Americans, across all 50 states.^{8,9}

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4. MOST DURABLE

Two frequent misconceptions about carbon pricing are that enacting the initial fee is the main political hurdle and the fee rate need not increase year to year. Neither is correct. For a carbon fee to meet agreed-upon emissions reduction targets, it must increase every year. British Columbia demonstrated this. When BC introduced a steadily rising carbon fee in 2008, emissions declined as intended. But when the carbon fee stopped increasing in 2013, emissions began rising again.¹⁰ Enacting a continually rising carbon fee that is immune to a popular backlash and to repeal efforts by future Congresses is a far greater political challenge.

The only way to guarantee this policy durability is by rebating the revenue directly to the American people, thereby creating a “hook” that cannot be undone. For example, the popularity of Alaska's dividend model turned it into a lasting program with decades of broad bipartisan support. Similarly, a national carbon dividends program may be the only climate solution capable of withstanding the political test of time. And this durability is a necessary pre-condition to strike a grand bargain capable of uniting Republicans and Democrats, businesses and environmentalists, and ultimately the American people, around a bipartisan climate breakthrough.

5. REGULATORY SIMPLIFICATION

The Baker-Shultz Carbon Dividends Plan is premised on a grand political bargain: trading a robust and rising carbon fee for a phase-out of most existing carbon regulations. Designed correctly, this would be a winning trade for all key stakeholders and a vast improvement over the status quo. For the past decade, US climate policy has zig-zagged between an aggressive regulatory agenda under President Obama to an equally aggressive de-regulatory push under President Trump. On-again-off-again regulation is a poor way to protect the environment or promote economic growth. A carbon fee offers a more cost-effective and business-friendly path to greater climate ambition.

Just as carbon dividends pave the way for a majority of Americans to support a carbon fee, they also make it possible for this grand bargain to take shape and sustain itself. Indeed, dividends can provide the glue to bind the deal together. For businesses and Republicans, dividends offer a uniquely popular and bipartisan pathway to significant and permanent regulatory relief. For environmentalists and Democrats, dividends would ensure that the carbon fee rate increases every year until emissions targets are met, thereby overcoming their resistance to regulatory simplification. If all parties believe the deal will last, the lack of trust separating them can be overcome.

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6. PRO-GROWTH

When combined with dividends, a carbon fee would become a pro-growth policy instrument with substantial stimulatory effects. The dividends would more than offset the negative effects on consumer purchasing power.¹¹ Since less well-off households consume a greater proportion of their income, carbon dividends would put money in the hands of those most likely to spend it, thereby boosting overall aggregate demand. A carbon dividends program would also incentivize households to reduce their energy costs by upgrading to cleaner cars and appliances, thereby spurring a new wave of consumer spending. This would in turn drive new business investment as companies sought to meet consumer demand.

A carbon fee would also send a powerful market signal that encourages technological innovation and large-scale substitution of existing energy and transportation infrastructures, stimulating new investment. The plan would also offer companies, especially in the energy sector, the predictability they now lack, removing one of the most serious impediments to long-term capital investment. Just as central banks rely on forward guidance to influence future market expectations, if investors know that a carbon price will increase steadily over time due to the popularity of dividends, the stimulatory effect of the final fee rate would be felt almost immediately for infrastructure and utility projects that have long-term paybacks.

7. RESTORING TRUST IN GOVERNMENT

Public trust in government is near an all-time low, at less than 20%.¹² This lack of faith in our government's ability to solve national problems further polarizes our body politic, empowering extremes at the expense of a sensible center. To a large extent, this worrying collapse of the center is rooted in a widespread perception among voters that our political and economic systems are rigged against their interests by wealthy, powerful and out of touch elites who control the game. Without restoring public trust in our political system, it will be difficult for the American people to unify around important national projects and a common narrative, and for our great nation to continue leading by example.

Carbon dividends offer a unique opportunity to channel this growing populist sentiment in a socially beneficial direction and demonstrate that we can solve national problems in a way that benefits all Americans. The new ground rules would make intuitive sense: the more you pollute, the more you pay; the less you pollute, the more you come out ahead. Since dividends are paid out equally to all citizens, your personal choices determine how much you pay and how much you benefit. This would tip the economic scales towards the interests of the many. As a result, carbon dividends could help restore trust in our public institutions and inspire a new sensible center in American politics.

“A carbon dividends program speaks to today's growing populist sentiment, and offers a unique opportunity to channel it in a socially beneficial direction

8. POSITIVE FEEDBACK LOOP

Political and economic systems – like natural and biological ones – operate on feedback loops, which can be positive or negative. Currently the dominant climate narrative is a negative feedback loop. Opponents often argue that solving climate change would constrain economic growth and impose undue costs on businesses and workers. Interestingly, much of the environmental movement's narrative reinforces a similar theme of shared sacrifice, along with dire warnings of climate catastrophe. What both narratives share in common is a message of fear and austerity: that climate protection requires short-term sacrifice. Not surprisingly, this negative feedback loop has yielded very modest emissions reductions.

A carbon dividends program offers the only climate solution capable of establishing a positive feedback loop that reduces emissions at the necessary scale and speed. Simply put: the more the carbon price increases, the greater the emissions reductions, and the higher the economic dividends to the American people. This favorable dynamic would encourage voters to support ever-greater climate ambition because it is good for their economic bottom line. From a political perspective, aligning individual self-interest with increased climate ambition changes everything. That is why the Baker-Shultz Carbon Dividends Plan would not only meet but exceed the US commitment under the Paris climate agreement.¹³

9. BORROWING BONUS

A carbon dividends program could be designed to expand consumer credit for specific climate related investments. Over half of all Americans do not currently have \$500 or more in savings. This prevents households from replacing old and inefficient vehicles, heating and cooling systems and appliances with more energy-efficient ones. Even though they would gain financially over the longer term by making these investments, they simply do not have the disposable income to afford large upfront purchases, or the access to affordable credit to make these purchases over time. Solving this problem could not only reduce emissions, but also spur economic growth by enabling households to make investments they otherwise could not afford.

Allowing individuals to borrow from private institutions against future dividend income streams for specific clean energy-related investments could become a key feature of a carbon dividends plan. With minimal regulatory intervention, this could lead to a new kind of consumer loan that gives more Americans access to affordable credit that lowers both their long-term costs and carbon footprints. For example, such a program could allow credit-constrained households to secure affordable credit to invest in more fuel-efficient cars, energy-efficient home improvements or new appliances. As a result, this could save money over time, while ensuring that even more Americans gain (or continue to gain) from a carbon dividends program.

“ Only a carbon dividends solution offers a bipartisan and politically sustainable pathway forward where all key stakeholders, above all the American people, can claim an important victory

10. CLOSING PANDORA'S BOX

As we have seen, there are many compelling reasons to return all carbon fee proceeds directly to the American people. Yet politicians will no doubt be tempted to use the hundreds of billions of dollars in new revenue for other purposes – whether it be paying down the debt, reducing corporate or personal taxes, investing in green infrastructure, or financing climate adaptation or remediation. While these other uses have merit and appeal to particular constituencies, they would each alienate many others. As tempting as it will be for elected officials to dedicate carbon fee revenues in these other ways, doing so would be a strategic misstep, and doom the political prospects of a lasting bipartisan climate breakthrough.

Each alternative revenue use would open a Pandora's Box. Whereas the Baker-Shultz Carbon Dividends Plan has already attracted an unusually broad and bipartisan coalition of support, no other use of proceeds can do so. Washington State learned this lesson the hard way: its attempt to pass a carbon fee failed largely because even its proponents could not agree on revenue use.¹⁴ At the national level, Members of Congress who pass a carbon fee that does not enjoy public support risk an electoral backlash, all the more so from a carbon fee that grows annually. Only a carbon dividends solution offers a bipartisan and politically sustainable pathway forward where all key stakeholders, above all the American people, can claim an important victory.

ENDNOTES

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