Overhauling our Tax Regimes for a Sustainable Future

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The purpose of taxes has long been established to help a polity function through material revenue raised from such taxes. Globally and historically, taxes have benefitted kingdoms, democracies, and theocracies in helping achieve their respective goals. Specifically, taxes help fund development and welfare projects, defense and militaries, scientific research, public insurance, salaries of government employees, the general operation of government, and public transportation. Taxes also help provide public goods and services, including better health infrastructure, development, and indeed, environment. The study of the latter, however, demands that we relook at our tax regimes.

In economics, the concept of externalities plays an important role in gauging the cost and value of a particular asset, service, or action. An externality typically means the unintended consequences of one's action that are to be borne by a third person who is not a party to the transaction. A positive externality occurs when a benefit spills over, while a negative externality occurs when such a third person suffers a loss. It is the negative externalities that define how inefficient environmental macro regulations and micro behavioral patterns may be. A simple example of a negative externality is the tailpipe emissions from one's car, which cause severe health impacts on others around, despite being external to the relation with the car. Such negative externalities affect us all and can be found aplenty. A positive externality can be seen in the case of apple orchards that help bees (which help pollination) survive, thereby promoting the outcome and produce of nearby agricultural activities.

The current tax regimes are based on and derived from the monetary rewards of citizens, natural and legal. These are employed in terms of income taxes, where a tax is imposed for the earnings they generate, GST, or Goods and Service Tax, for services they provide, and, among others, import and export duties for contributing to, and of course, benefitting from global trade in terms of the respective goods and services. Taxes thus, quite literally, tax the positive outputs in order to further generate revenue for the governments from the revenue generated by the citizens. A positive and rewarding act is taxed. This is opposed to a negative, unlawful, or illegal act that is fined.

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To achieve global sustainability, there is a need for holistic and urgent revamping of such tax structures. The 2022 Declaration can contribute to developing this process. As revenue generation is imperative and indispensable for governments, policies should be promulgated where environmentally negative externalities should be taxed, while the positive outcomes of honest human actions with positive externalities should be rewarded. This would mean that actions that promote negative externalities, including wastage of water, generation of solid industrial and municipal waste, air pollution through industrial activities, or otherwise, change in land use from environmentally beneficial ecosystems to industrial or residential and the like, need to be taxed. Such taxes, gradually, would reflect a change in value systems and behavioral patterns of the population. This would also directly disincentivize citizens towards undertaking actions that would have negative consequences on the environment.

A common example of such a taxation regime is the carbon tax, where the emitter is taxed based on the amount of carbon (carbon dioxide) that is directly put in the atmosphere by him. A carbon tax can theoretically create a net gain to world society over the long term as it provides an incentive to reduce emissions directly and encourages the search for alternatives to carbon energy (Helm, Dieter, The Carbon Crunch, New Haven, Yale University Press, 2012). A more basic principle under which the carbon tax could be clubbed is the Polluter-Pays principle. It is the principle used to allocate costs of pollution prevention and control measures to encourage rational use of scarce environmental resources and to avoid distortions in international trade and investment. It needs to be strengthened in the context of the 2022 Declaration but also adapted to consider the regime overhaul suggested in this article. For instance, the owner of an internal combustion engine vehicle may be taxed higher in terms of the registration fees and road tax, fuel prices, parking tickets, and the like, while the owner of an electric vehicle may be given proportional rebates.

Of course, valuing negative environmental externalities comes with its own set of challenges. How does one value the cost of carbon put in the atmosphere, where it could cause physical impacts on health, cognitive abilities, focus, and increase in human errors? The concept of ecosystem services adds to this debate. These services can be seen as contributions of ecosystem structure and function (in combination with other inputs) to human well-being. Furthermore, much like financial risk management, which governs the price and demand of a financial utility, environmental risk management also would imply and govern the fluctuation of the cost of a specific externality that embroils the mechanism further.

These arguments, about the complexities of a possible overhauling of global tax regimes to reward positive actions that lead to human income, and tax actions that generate negative environmental externalities, are not new and commonplace for every amendment and new provision. What is required, and what the 2022 Declaration should promote, is an approach that looks to reestablish consumer, industry, and supply chain behavior to reflect the true environmental cost of that action. Human beings have exploited the environment for too long, and the solution lies in the market dynamics of taxation and incentivization in favor of sustainable living.

[1] Externality is a kind of “missing market” (Arrow 1969) – an unpriced effect that upsets the assumption of the complete system of markets – and its formalization is achieved by introducing a direct interdependence between utility or production functions. Arrow, K. J., “The organization of economic activity: Issues pertinent to the choice of market versus non market allocation”, *Congress of the United States, The Analysis and Evaluation of Public Expenditures*, The PPB System, 1969, pp. 47–64.

[2] Wealth Tax, Property Tax/Capital Gains Tax, Gift Tax/ Inheritance or Estate Tax, Corporate Tax, Service Tax, Customs Duty, Excise Duty are some of the other prominent taxes.

[3] Guiding Principles Concerning International Economic Aspects of Environmental Policies, annex, Organization for Economic Cooperation and Development (OECD) Doc. C(72)128 (May 26, 1972)