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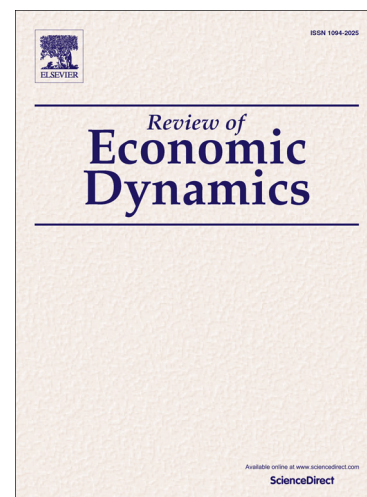
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# The Distributional Effects of a Carbon Tax on Current and Future Generations

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## Abstract

This paper uses a life cycle model to compare how different approaches for recycling carbon tax revenue affect the welfare of agents born in the future steady state versus agents alive when the policy is adopted. Our results demonstrate that the welfare consequences of a given policy vary substantially across these two groups. For agents born into the future steady state, the expected non-environmental welfare costs are minimized when carbon tax revenue is used to reduce an existing distortionary tax. In contrast, among the agents alive when the policy is adopted, recycling revenue through uniform, lump-sum rebates results in the largest welfare increase across the policies we examine. Moreover, we find that the regressivity or progressivity of a policy also differs within the living population versus the future steady state population. Overall, our results illustrate that estimates of the non-environmental welfare costs of carbon tax policies that are based on the long-run outcomes miss-represent the near-term consequences. Given the potential importance of these near-term effects on the political feasibility of a policy, our findings indicate that, when designing a carbon tax, policy makers must pay careful attention to not only the long-run outcomes, but also to the transitional welfare effects of the policy.

Keywords: Carbon taxation; overlapping generations

JEL codes: E62; H21; H23

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