



IES/IEEP Policy Forum

# Prospects for an Environmental Tax Reform

**Samuela Bassi – IEEP**

[sbassi@ieep.eu](mailto:sbassi@ieep.eu)

[www.ieep.eu](http://www.ieep.eu)

Brussels, 15 June 2009

# Content of the presentation



- ❖ Study on ETR: overview
- ❖ Focus: Acceptability and feasibility of ETR
- ❖ ETR today – trends & examples
- ❖ ETR possible future scenarios
- ❖ The issue of harmonisation – enhanced cooperation and OMC
- ❖ The questionnaire
- ❖ Key findings
- ❖ Way forward

# The study on ETR



*'Tax Reform in Europe over the next decades: implication for the environment, for eco-innovation and for household distribution' for the **EEA***

**Objective:** identify environmental taxes/charges (and associated use of revenues) that stimulate **eco-innovation** and contribute to **competitiveness**, **distributional equity** and **environmental benefits**

## Tasks:

- **A: Eco-innovation** >> promotion of green industry + impact on employment
- **B: Distributional implications** >> ETR implications for households
- **C: Feasibility implementing a radical ETR and its acceptance**  
>> *the focus of this presentation*

**Partners:** Kommunalkredit Public Consulting



Cambridge Econometrics,



Gesellschaft für Wirtschaftsforschung



Ecologic



Policy Studies Institute



King's College London



Institute for European Environmental Policy



Institute for European Environmental Policy

# FOCUS: Task C - Acceptability and feasibility of ETR



**Aim:** Analysis of legal feasibility and political acceptability of a radical ETR in the context of EU policies.

- Explore what radical approaches for ETR exist & their potential feasibility – focus on ‘enhanced cooperation’, and ‘open method of coordination’ (OMC)
- Explore what experts see as the need and potential for ETR – is there scope for a radical shift in the tax burden? Are radical solutions needed?

3 aspects

**Legal:** possibilities and legal implication of enhanced cooperation

**Political:** Open Method of Coordination (OMC).

**Social:** perceived potential and barriers of ETR

Info basis: Literature + inputs from **questionnaire and interviews**

# ETR today – Uneven approach in EU



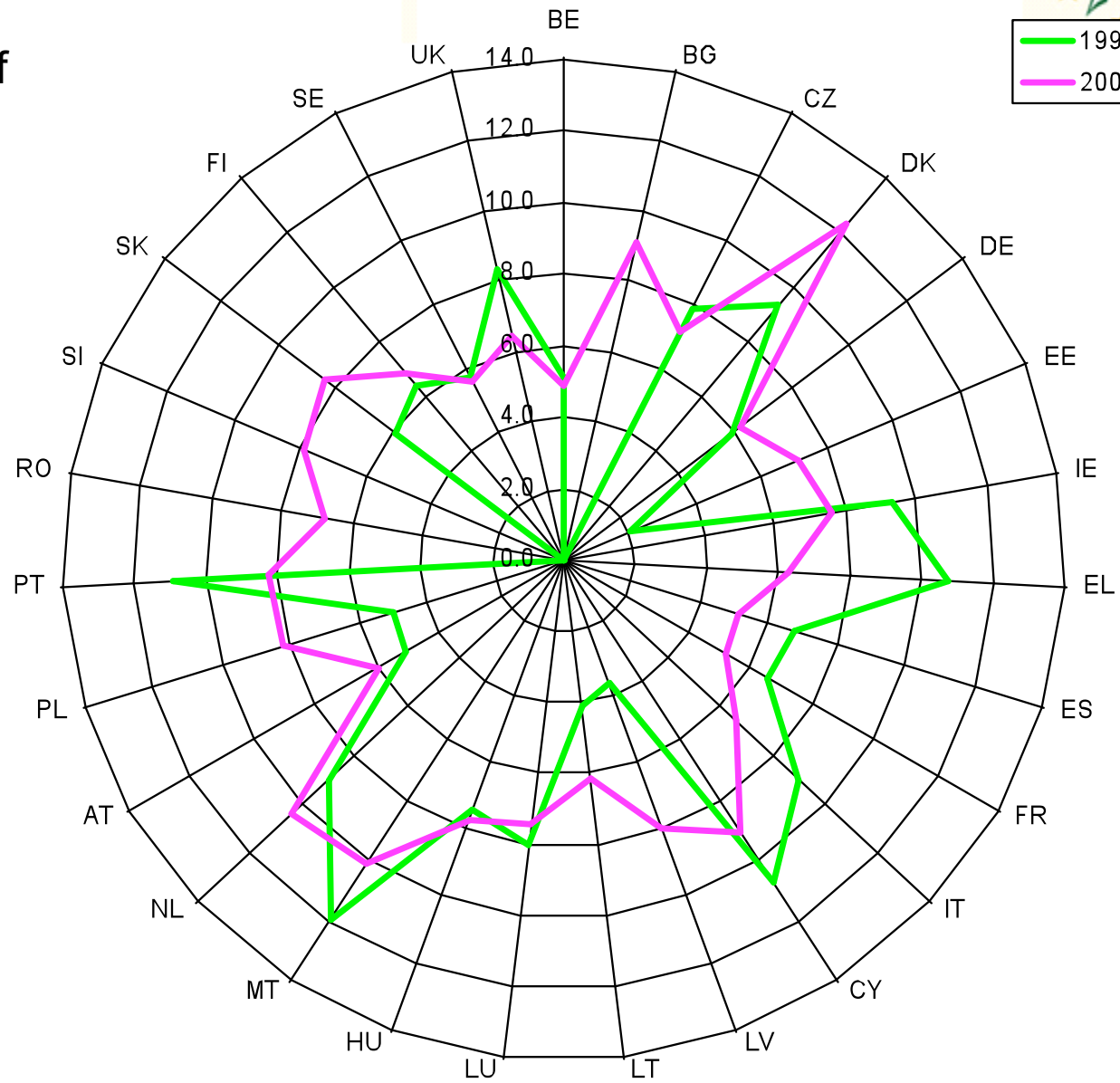
- **ETR applied by some MS:** FI (1990), SE (1991), DK (1993) NL (1996), UK (1996), SL (1997) AT (1994), DE (1999)
  - Other MS have implemented environmental taxes, but not a full ETR.
- **Level of green taxes also uneven:**
  - Some countries have higher share of env taxes (over total tax revenues) – e.g DK (12.2%), NL (10.4%), MT (10.1%) in 2006
  - Other countries less keen – e.g. FR (5.2%) ES (5.1%) BE (4.9%)
- **Trends:** EU average increased in the 90s (up to 7%), slightly decreasing now
  - **6.7 %** in 2006

- **Low uptake – full potential yet to be explored**
- **Organic approach to ETR never been developed at EU level so far**

# Green taxes trends in EU



Env taxes as **share** of total tax revenues  
1995 -2006



Source: based on data from Eurostat (European Commission, 2008)

# Example of ETR - SE (1991)



- First introduced in 1991
- 10-year tax-shifting programme (2001–2010)
- Reduction in personal income tax and social security contributions
- Environmental and energy taxes including **CO2 tax, SO2 tax, tax on diesel, electricity** (industry + households), **pesticides**
- EUR 3.3 billion >> 1.4 % GDP shift by 2010

# Example of ETR – DE (1999)



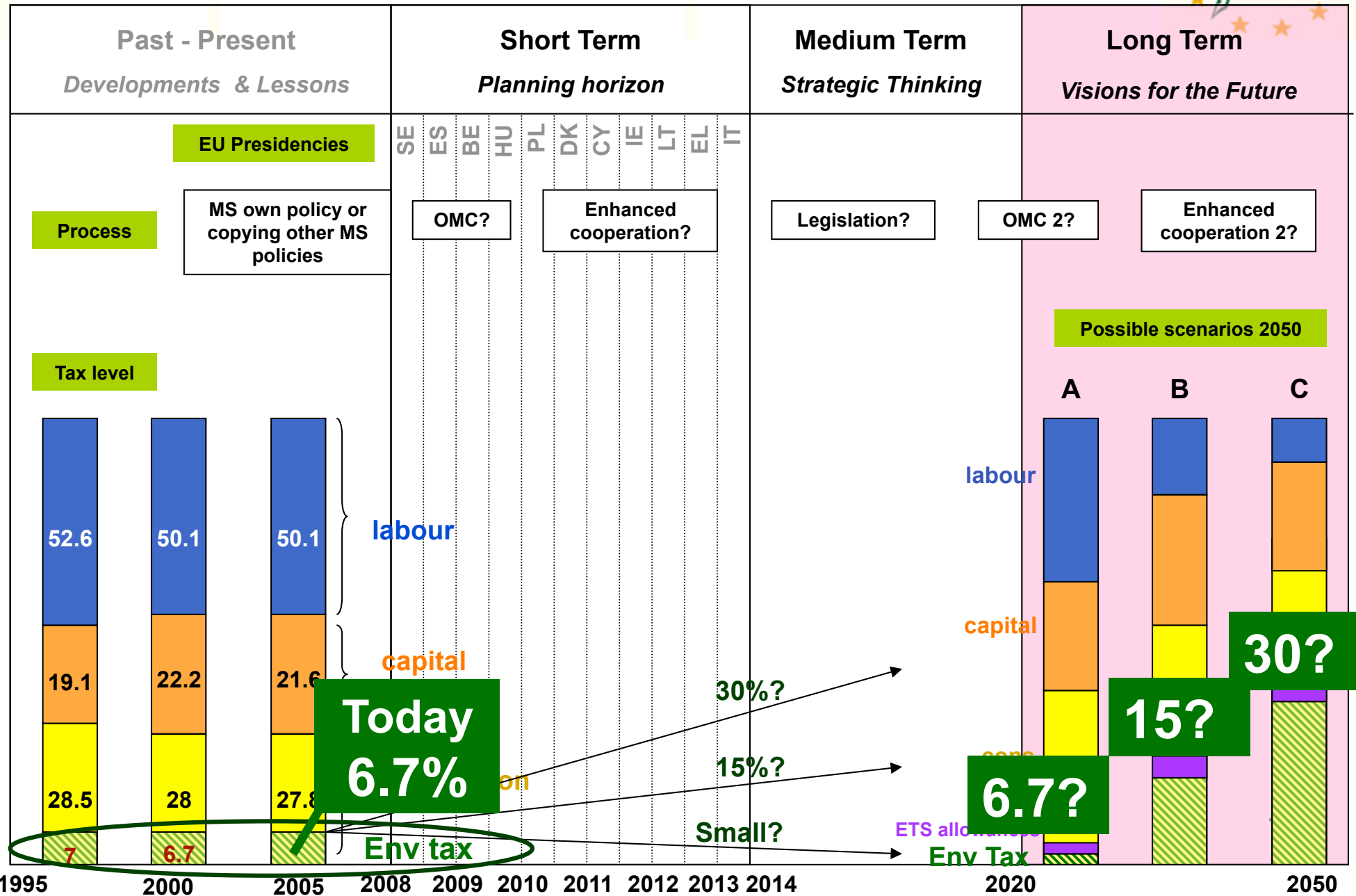
- **2 objectives:** env protection (espec. GHG) & reduce pension contributions
- Stepwise increases in **taxes on transport fuels** (petrol and diesel) and other energy products over 5 years + **electricity tax.**
- Special **tax rebates for some sectors** (eg energy intensive)
- Env tax increase offset by **1.7 % reduction in pension contribution.**
- In principle **revenue neutral** – except 1% increase to promote RES
- **Acceptance** rose and fell over the years – most criticism from industries, espec. in period of higher oil prices
- **Impact:** considered successful – reduction of car use

# Example of ETR – UK (1996)



- Landfill levy (introduced in 1996), climate change levy (2001) and aggregates levy (2002)
- recycled back to the economy via a **cut in employers' national insurance contribution**
- **Revenue-neutral.**
- A **small part of the revenues** hypothecated for **setting up specific funds** (e.g for research projects and investment schemes)

# ETR – Possible future scenarios



# The issue of harmonisation



The European Council has power to *‘adopt provisions for the harmonisation of legislation concerning indirect taxation to the extent that (...) is necessary to ensure the establishment and the functioning of the internal market’*. (Art 93 TEC)

**i.e.: Council needs to act unanimously**

**>> few EU measures contributing to ETR adopted so far**

# Pathways for harmonisation



Legal approaches across all EU

- Legislative specific minimum requirement:** energy tax directive, VAT
- Legislative general requirement:** 'principle of recovery of the costs of water services' under WFD for water pricing
- Legislative possibility:** Eurovignette

Harmonisation

Legal approaches for a subset of MS: **Enhanced cooperation**

- Special legal framework:** e.g. initial Schengen >> limited no of MS under international treaty distinct from EU treaties.
- Existing legal framework:** eg **Enhanced cooperation** under EU Treaties – never applied. Schengen/EMU incorporated into EU legal frame with opt-outs

Political intention to promote ETR: **Open Method of Coordination (OMC)**

- Formal/structured OMC** e.g. Lisbon Strategy, Broad Economic Policy Guidelines (incl. ETR)
- More flexible/light OMC** – e.g. *Green public procurement (GPP)*
- Voluntary policy coordination** e.g. *Cars-CO2; reform of EHS*

Learning from others (copy-cattng)

- Based on **other MS' initiatives** – e.g. use of revenue neutrality
- Own needs and **own initiatives** – e.g. ETR in UK Landfill tax

# Open Method of Coordination (OMC)



- **Framework for cooperation** between MS
- Help drive national policies towards **common objectives**.
- In **areas which fall within the competence of the MS** (incl. and fiscal measures).
- It usually focuses on: jointly identifying and defining **objectives** to be achieved, **measuring instruments** (eg indicators, guidelines); **benchmarking**
- ‘Soft law’ measures: **political commitment** but not legally binding.

In practice: **used in different policy areas** e.g.

- SDS, European Climate Change Programme (ECCP), Common Implementation Strategy of the Water Framework Directive (CIS-WFD), Seville Process (IPPC), GPP etc.

# Enhanced cooperation



- It allows a **group of MS (min 8)** to work more closely on certain matters, within EU legislative framework
- Other MS can join later if they wish
- It should not undermine the common market
- Needs authorisation of the Council
- **Last resort measure**, i.e. when common action under Treaties not possible within reasonable period.

>> It requires a *de facto* admission of failure of the EU institutions to deal with some matters

In practice:

- **Not used so far.**
- Similar processes: Schengen and Euro area

# The questionnaire



About 15 questions to experts, EC, MS, NGOs, associations, other bodies (eg OECD)

## Key Qs:

### ❖ *Future policies and scenarios*

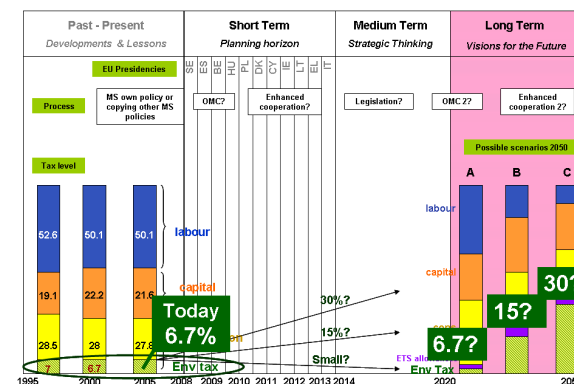
- Are environmental taxes useful?
- For which policy areas (climate, water, air, biodiversity etc)?
- What increase of env taxes feasible by 2050 -2020-2010?
- Interaction with EU ETS (auctioning)?

### ❖ *Harmonisation process*

- What scope for enhanced cooperation and OMC?
- What MS most keen?

### ❖ *Acceptability of ETR*

- Winners and losers?
- Past lessons?
- How to overcome barriers to ETR?
- What messages to communicate?



**Still open  
for  
comments!**

# The questionnaire (2)



Feedback received so far:

~ 30 replies

From inter alia: DG Env, DG Taxud, DG Ent, EEA, JRC, OECD, Member States (IT, EE), NGOs (EEB et al) and other experts

Some more to come

# Key preliminary findings - **Visions** for the future of ETR



Many experts see a **doubling** of environmental taxes' contributions to tax revenues (from 7% to 15%) by 2050 as appropriate and feasible.

*However:*

The ETR shift is not expected to start in earnest in the short term (with some exceptions) given lack of political courage.

# Key preliminary findings – **Areas of applicability**



- **There are a number of new & existing areas that can contribute to ETR**
  - **Major scope for** carbon taxes, landfill taxes, pollution taxes, circulation charges, product taxes, natural resource charges
  - Scope for **revising and extending existing instrument** – e.g. level of excise tax, level of auctioning, landfill tax rates.
  - Scope for **new instruments** – such as landuse / maritime fuel taxes.
  - **Biodiversity:** increased recognition of risk of bd loss >> fertilizer, pesticide taxes, water abstraction charges/pricing etc
  - Scope for **leverage** – e.g. link structural fund allocation to green taxes.
  - Include subsidy reform

# Key preliminary findings - Harmonisation



- ❖ **Enhanced cooperation** ok in principle but looks impossible in practice
  - The current requirements can be politically sensitive
  - There is currently no appetite for reforming the rules.
  - There may be a need and opportunity in the future –eg with treaty changes needed as EU enlargement continues.
  
- ❖ **Open Method of Coordination (OMC)** less controversial & already been applied on many policy areas. However it may be a weak tool
  
- >> **'copying others'** will offer some benefits and should be encouraged
- >> Need for a strong(er) **politically led commitment** to ETR/EFR
- >> strong(er) commitment to **OMC** needed
- >> need to look again at **enhanced cooperation?**  
... for the 15% by 2050 to be reachable.

# Key preliminary findings - **Acceptability**



## Right structure:

- Enabling condition: Right **design** (eg gradual introduction) needed
- Implement env taxes as part of a **package of instruments**

## 'Sell' the message:

- **Linking** tax / charge rises **to use of the revenues**
- **Linking** tax rise with **social security/employment** taxes (even if scope limited)
- **Communicating the benefits** has proven useful (e.g. DE, MT)
- Some noted that **the word 'Tax'** in ETR difficult to sell!

## Social implications:

- **Affordability** needs to be factored in
- Social acceptability likely to be **influenced by e.g. extreme env events** (climate change, droughts, resource scarcity etc) & **economic changes** (e.g. financial crisis).
- **Encouragement of EU** to help motivate less "ETR-keen" MS & raise awareness

# The way ahead



- Need for **long term vision/strategy** with objectives and targets
- **Commitment to 'get prices right', PPP, UPP and full cost recovery**
  - Systematic look at where taxes and charges can be applied – policy areas, countries with opportunities
  - Apply (with due care) what works elsewhere
  - Build on existing instruments – eg fuel tax escalator
- A **target** is helpful - e.g. of 1% per year env tax increase
- Look for **policy synergies** (climate change, water stress)
- Commitment to **at least a 'strong' OMC** at EU level and collaboration internationally.
- **Opportunities** - SE to promote carbon tax during EU presidency. FR proposing ETR – *Success depends on champions*

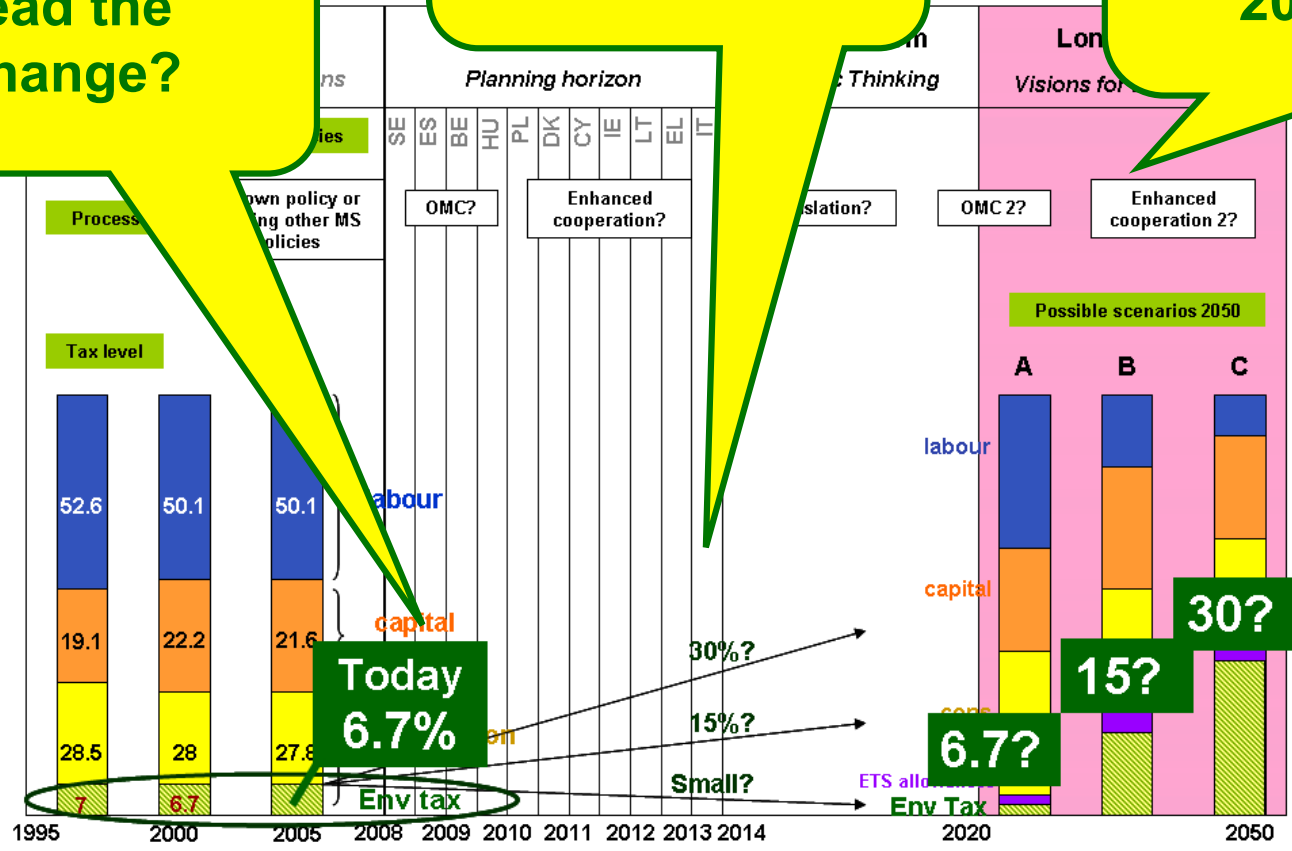
# Questions to you



Who is going to lead the change?

What radical approaches will allow change?

What is a needed ETR share? What is feasible – 2020, 2030, 2050 ?





# Thank you

For further info please contact: [sbassi@ieep.eu](mailto:sbassi@ieep.eu)

*'IEEP is an independent not for profit institute dedicated to advancing an environmentally sustainable Europe through policy analysis, development and dissemination.'*

[www.ieep.eu](http://www.ieep.eu)

# What is ETR?



**Environmental tax reform (ETR)** is

*‘a gradual **shift of the tax base** away from taxing **‘good resources’** such as investment and labour, toward taxing **‘bad resources’** such as pollution and inefficient use of energy’* (EEA, 2005).

From taxing **GOOD** (labour) to **BAD** (pollution)

↓ Labour taxes >> ↑ Environmental taxes

**Environmental Fiscal Reform (EFR):** broader concept - includes reform of environmentally harmful subsidies (EHS) - (not covered in this study)

# Environmental taxes



**Taxes:** compulsory payment levied on a tax base (e.g. labour, consumption, capital) – amount is a political decision - revenues can be used for different scopes (e.g. VAT)

**Charges/fees:** amount based on costs/benefits (e.g. cost of water provision) - revenues are earmarked

Some examples of taxes & charges:

**Air/Energy:** CO<sub>2</sub>, SO<sub>2</sub>, NO<sub>x</sub>, fuels

**Transport:** Car sales/registration taxes, annual car circulation tax

**Water:** water pollution, water abstraction charges

**Waste:** Landfill tax, dangerous waste

**Noise:** Aviation noise

**Natural resources:** Gravel, Sand, Land use charges

**Products:** Tyres, Plastic bags, Fertilisers etc

# Key “buzzwords” within ETR debate



- The ‘**double dividend**’: improvement in both the environment (by properly pricing externalities) and to the economy, by making cost of labour cheaper hence encouraging employment – *this is the specific ambition; but “single dividend” ETR should not be ignored*
- ‘**revenue neutrality**’ - often associated to ETR: additional revenues from env taxes used to decrease revenues form other taxes so that the overall tax burden remain the same - *this is a tool for public acceptability, not a fundamental need for ETR..*