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COMMENTS ON THE GREEN PAPER ON MARKET-BASED INSTRUMENTS FOR ENVIRONMENT AND RELATED POLICY PURPOSES – COM (2007) 140

1. Introduction

1.1. BUSINESSEUROPE welcomes the Commission's initiative to launch a discussion on advancing the use of market-based instruments (MBI) in the European Community. The EU currently faces enormous environmental challenges, which can only be countered by ensuring sustainable economic and environmental development on a global scale. Efficient energy consumption, on the one hand, which can contribute to improved competitiveness and innovation potential for Europe's companies, and the protection of the environment, on the other hand, are key goals in this respect.

1.2. The Green Paper focuses to a considerable extent on taxation as an instrument to address these challenges. Environmental taxes, however, are only one instrument available to policymakers to combat environmental problems, and are, in our view, in most cases, not the most efficient one. This is due, inter alia, to the high tax levels that are often required to achieve environmental goals. In addition, taxes pose significant risks to the global competitiveness of European companies if their application is restricted to the EU. There is a whole range of other MBI which we believe are, in most cases, more effective and less distortionary on the global scale, and that should be given more consideration in the current debate.

1.3. Furthermore, the Green Paper stresses the revenue-raising potential of green taxes. In our view, taxation for budgetary reasons is a different topic from taxation for environmental reasons, and the two should be dealt with separately. Companies have taken note of the current discussion on whether energy taxes could contribute to a much-desired lowering of economically detrimental taxes on labour. They would thus not only serve environmental purposes, but also employment-raising goals ("double dividend"). Recent research, however, has shown that such double dividends are not likely to occur, unless very specific assumptions are made concerning the tax structure and the way the economy is functioning. As a consequence, consensus opinion now holds that environmental taxes should be used exclusively to correct environmental problems, whereas unemployment and other policy issues should be handled with instruments that are specific for those problems.

1.4. MBI can play an important role in achieving environmental aims. They influence the price of products and can thus provide the desired incentives for a more efficient use of resources and for waste reduction and for a better control of the environmental impact, while guarding a level playing field between different products. It has long been recognized in economic theory that MBI are usually more efficient policy instruments than regulatory measures for internalizing undesired effects of energy consumption and fuel combustion. This is to a large part due to the flexibility they provide regarding possible adjustments and differentiation according to the user, which can lead to a reduction of internalization costs.



2. General evaluation

2.1. In our view, EU-wide policy harmonisation should focus on those environmental problems that are common to all member states and that do not respect national borders, such as greenhouse gas emissions. The environmental impact of greenhouse gases does not depend on the location or on the source of the emission. Thus, a cost-efficient way to combat problems caused by greenhouse gas emissions is a harmonised policy. The EU Emissions Trading Scheme (ETS) is one example of an attempt to harmonize policy in such an area.

2.2. In contrast, the way in which individual countries are using the revenues from CO₂ taxes (or the revenues from the auctioning of permits) should not be an EU issue, but rather a question for each country. There is no obvious reason why the use of public funds should be harmonized. On the contrary, there are strong arguments in favour of taking decisions on public spending at the national level since the structure of the public sector differs significantly between countries, due to differences in demand.

2.3. A general conclusion therefore is that the discussion in the Green Paper concerning a concerted action plan for energy tax reforms is too optimistic and in some cases not even desirable. BUSINESSEUROPE would like to point out the large differences in tax bases for energy taxes and for labour taxation. Hence, not much can be achieved in terms of reduction of labour taxation by raising green taxes.

2.4. Concerning the greenhouse gas area, we do not believe that the introduction of additional or higher energy taxes, in addition to the prevalent instrument in this area, the ETS, would be effective. First of all, the functioning of the ETS needs to be improved. Alternatives to the envisaged auctioning system, such as use of a benchmarking system, need to be explored. The ETS could also be extended to other countries where this is appropriate, in particular outside of the EU. There might be a need for additional policy measures to cut emissions in sectors not covered by the ETS. This should be left to national governments to decide.

2.5. For the moment there are some obvious obstacles to an efficient control mechanism of greenhouse gas emissions. One is that some of the Member States which are part of the ETS still have national CO₂ taxes, on top of the EU ETS. This creates inefficiencies in the sense that CO₂ reduction measures will not be allocated in the least expensive way. In such a case, the cost for CO₂ reduction will be higher than necessary for the EU.

Double regulation should always be avoided. There should be no minimum taxes for fuels used by firms under the ETS, and electricity produced under the ETS regulation should be excluded from minimum taxation, as the price of the emission allowance is already included.

2.6. For many other environmental problems that are more local in their character there is of course room for national tax reforms. But this is not a question for the Community but for the individual countries.

3. Specific comments to questions posed in the Green Paper

3.1. What are the areas and options for the further use of MBI at EU or national level?

The further use of MBI has to respect the following principles:

- MBI must provide predictability and legal certainty for business investments; they should thus be introduced for the longer term,
- the instruments used should be effective in reaching the agreed objectives,
- the instruments should be economically efficient and the costs of reaching the objectives should be as low as possible,
- negative effects should be minimized, MBI should not impact on the international competitiveness of European businesses,
- there should be no overlap of different MBI,
- MBI should be easy to administer for authorities and businesses,
- MBI should not be open to diverging interpretations.

3.2. Could market-based instruments be used in a way that promotes competitiveness and does not impose an undue burden on consumers, in particular citizens with a low-income, but at the same time ensures revenue for public budgets?

Competitiveness could only be maintained if Europe's trading partners face similar costs in their own countries. Otherwise EU companies, especially in the manufacturing sectors, might be inclined to transfer their business outside Europe, and, at the global level, the amount of emissions will not decrease, but further increase.

Environmental policy instruments, market based or not, will, in general, not promote competitiveness.

Taxation and the EU ETS generally increase the cost of doing business. Thus, at least in the short term, they weaken competitiveness. By implication, public revenue will decline. This burden will ultimately be carried by the final consumer.

BUSINESSEUROPE (then: UNICE) published specific design and test criteria in September 2002 (attached).

3.3. Should the EU more actively pursue taxation to further Community policy purposes (in addition to fiscal objectives)? Is this the right response to current global challenges and the fiscal needs of national budgets?

The greenhouse gas area is an area where MBI can be developed further. Again, eliminating inefficiencies in the ETS is a good starting point. In general, since a great number of tax policy areas are in the fiscal sovereignty of member states it would be useful to analyse carefully whether the current allocation of competences is adequate. On the whole, as mentioned earlier, fiscal objectives should not be coupled with other policy objectives.



3.4. Should the EU more actively promote environmental tax reforms at national level? How could the Commission best facilitate such reforms? Can it for example offer some kind of co-ordination process or procedure?

On environmental policy in general, the Commission could provide a forum for the exchange of information between member states, in order to improve consistency between the national initiatives and prevent undesired cross-border effects. This forum should not be restricted to exploring the potential for further green tax reforms. Rather it should carefully analyse all instruments available as to whether they are adequate, cost-efficient and effective in reaching the desired targets. In general, EU policy must not hinder national efforts to explore avenues other than taxation to combat environmental problems.

3.5. Would the establishment of the abovementioned MBI Forum be useful to stimulate exchanges of experience/best practice on Environmental Tax Reform between Member States? How could it be organised in an optimal way? How should it be composed to avoid potential overlap with existing structures?

The involvement of business organizations at EU and national level should be ensured.

As already mentioned, environmental taxes, however, are only one instrument available to policymakers to combat environmental problems, and are, in our view, in most cases not the most efficient one.

3.6. How does the need to reduce the tax burden on labour in many Member States fit with the objective to promote innovation and to support research and development in order to shift towards a "greener" economy? How can this be achieved while at the same time respecting the budgetary neutrality? Would a more significant tax shift towards environmentally damaging activities be the right answer?

Again, this discussion should not be dealt with in the context of the Green Paper on MBI for environmental purposes. There is, in our view, no trade-off between environmental and labour taxation. Shifting taxes from labour to pollution and energy will mean in practice replacing a direct tax on labour by an indirect tax.

Decreasing the cost of labour has significant positive dynamic effects on labour supply and economic growth. This partly neutralizes the negative budgetary effects without having to take recourse to another source of taxation. The budgetary effects of environment taxes on companies would not be favourable due to harmful effects on competitiveness and growth. This would also encourage companies to invest outside Europe which would have negative effect on the labour tax base.

As a general rule, BUSINESSEUROPE considers that the reduction of the taxation on labour should be compensated by a reduction of public expenditures and by an actual reduction of the overall level of taxation.



3.7. What is, in the light of national experiences, the best way to advance the process of reforming environmentally-harmful subsidies?

The concept "environmentally harmful subsidies" is not clear. Subsidies should always be evaluated both from an economic and an environmental point of view.

A general problem with subsidies is that they create "rent seeking". Subsidies for energy-saving investments might create incentives to overinvestment. Normally, a substantial reform of the policy area in question would be a more efficient solution.

3.8. Should the Energy Taxation Directive be reviewed to make a clearer link to the policy objectives the Directive integrates, in particular in the field of environment and energy? Would this make energy taxation a more effective instrument by better combining the incentive effects of taxation with the ability to generate revenue?

Any review must be undertaken in the context of the broader policy framework, including consideration of the whole range of MBI available. It must take into account the impact on the global competitiveness of Europe's companies, and should not be conducted primarily with a view to revenue-raising.

The Energy Taxation Directive has to take account of the ETS trading system. There should be no minimum taxes for fuels used by firms under the ETS, and electricity produced under the ETS regulation should be excluded from minimum taxation, as the price of the emission allowance is already included.

3.9. Is splitting the minimum levels of taxation between energy and environmental counterparts the best way for doing so? What would be the pros and cons and the main practical aspects of such an approach? Would the environmental incentive created by energy taxation be a sufficient and adequate response to reflect the objectives of the energy policy in the field of biofuels, including the creation of a market-based incentive for second generation biofuels?

The idea of splitting the minimum levels of energy taxation between energy and environmental counterparts calls for further research. However, it should be noted that direct or indirect overlap of two different instruments (e.g. such as taxation and EU ETS) should be avoided.

All biofuels must follow the principles of a technology-neutral and performance-orientated approach in a non discriminatory way. Any scheme to categorize the performance of any biofuel (categorized as of first or second generation) should focus on encouraging and supporting biofuels based on the sustainability performance ("Well-to-Wheels" greenhouse gas emission and performance, as well as social, economic and environmental factors associated with feedstock production).

Therefore any market mechanism or any regulatory instrument must facilitate the most cost-effective option for greenhouse gas emission reduction, and ensure that any scheme to categorize the performance of biofuels is based on sound "Well-to-Wheels" principles: simple, transparent and practical to manage.



BUSINESSEUROPE does not support the current application of tax incentives on biofuels throughout the EU, since the lack of harmonisation of excise duties across Europe leads to an inherent lack of harmonisation of biofuel incentives. As this is currently the case, an extension of such an approach to advanced biofuels would hamper the development of this sector. The use of excise exemptions is inherently linked to overall fiscal policy, and therefore it is difficult to provide the markets with the necessary long-term certainty necessary to encourage investment.

3.10. Is there a need for additional taxation addressing the remaining environmental aspects of electricity production (if any)? Is the proposed approach sufficient to favour uptake of electricity of renewable origin? What is the impact of such a Community framework for electricity of nuclear origin (bearing in mind the differing approaches at national level towards the use of nuclear energy)?

There should be one single instrument in place to address a specific environmental problem. Overlapping of instruments must be avoided. The instrument must provide the predictability required by companies for long-term business investments.

3.11. Would the suggested changes to the Energy Taxation Directive and the proposed approach to its scope be the best solution for ensuring coherence between the Directive and EU ETS? Are there other options to achieve this objective?

ETS is the core instrument for addressing the challenges posed by climate change, but it should not necessarily be extended to other areas. BUSINESSEUROPE has commented on the role the ETS could play in the future and on how best to develop the ETS scheme in its recent paper on the ETS review (attached).

3.12. What are the potential options that should be explored in order to provide the necessary incentives to encourage the EU's trading partners to undertake effective measures to abate greenhouse gas emissions?

This question should be debated in other multilateral fora.

3.13. What would be the best MBI to tackle emissions from shipping, taking into account the specific nature of maritime transport? How could it be best designed?

Emissions of maritime traffic should be taken care of on a global level in order to avoid distortion of competition. The IMO (International Maritime Organisation) has an important role in this process. Any policy instrument needs to be evaluated as to its cost impact on the maritime sector. Different solutions are required depending on whether emissions have a local, regional or a global effect.

3.14. How can infrastructure charging, including considerations related to environmental costs, best be applied to transport modes? Should this model apply to all transport modes, or take into account specificities of each transport mode? To what extent should the Eurovignette directive be used in this respect?



If the current tax system will be altered, it is important to take into account different modes of transportation. Also we have to take into account the specific circumstances of different member states. For instance, decisions on whether or not to introduce road pricing is best left to the member states, as the traffic density varies significantly between countries. The subsidiarity principle should serve as guidance in this debate

3.15. How can the Commission most effectively ensure implementation of the water pricing policies set out in the Water Framework Directive? What options could be explored to reinforce the links between investments in national water projects and the introduction of corresponding water pricing to provide incentives for users and avoid distorting competition?

We do not support further MBI with regard to water pricing, to the extent that national systems might already fulfil the “cost recovery” and “polluter pays” principles required by water framework directive.

3.16 If there is insufficient progress to divert waste away from landfill, should the Commission consider proposing a harmonised landfill tax with EU-wide minimum rates?

Does the Community legal framework provide sufficient scope for Member States to use MBI to address waste management issues? Should the Commission facilitate the application of MBI in this area, e.g. through supporting exchanges of information?

There should be no harmonization of a landfill tax within the EU. Member States should be able to take care of these issues on a national basis. The social cost of dumping waste in landfills differs substantially between member states, depending on many factors. The social cost of using landfills in less populated Member States is probably very different from more densely populated countries. Thus it would be very inefficient to harmonize taxation.

3.17. Should the Member States make a more intensive use of these types of instruments? Should, in particular, "payments for environmental services" be used more intensively to achieve environmental objectives? And should the scope for introducing systems of biodiversity offsets at Community level, e.g. wetland banking, be further examined?

Due to measurement and valuation problems, we consider the further use of MBI in this area difficult.

3.18 Do you see scope for using cross border emissions trading schemes between groups of Member States to combat conventional air pollution through SO₂ and NO_x? How should such a system be designed to fit with national taxes and charges that are applied in several Member States?

Trading systems are problematic for several reasons. A major problem is that such systems demand permit trading that is not based on a “one to one basis”. Due to this, an efficient system would be fairly complicated.



Another problem is that some member states have explicit sulphur and NO_x taxes/charges. Those have to be considered in such a trading system.

NO_x and SO₂ should be regulated under the IPPC directive, using tools which are already available. Because of the regional effect that these pollutants produce, a hypothetical ETS for NO_x and SO₂ would not solve the environmental problems that they may create. Furthermore, the conditions for a free and fair market of NO_x and SO₂ are not met. If, however, eventually the ETS for NO_x and SO₂ would be introduced in the proposal of reviewed IPPC directive, we would insist on two conditions to be fulfilled: the option to implement it shall be left up to Member States; and the freedom to participate in such a national or regional ETS shall be left up to the level of any IPPC permitted installation.

Overlapping of different trading or permit systems should be avoided in all cases. Therefore, we do not support the idea of several different MBI addressing the same environmental problem.