Green Paper on market-based instruments for environment and related policy purposes

2007/2203(INI) - 28/03/2007 - Non-legislative basic document

PURPOSE: to present a Green Paper on advancing the use of market-based instruments in the Community for environment and related policy purposes.

BACKGROUND: the EU has taken a global lead on climate change as well as on the use of environmentally sustainable policies. To date the EU has favoured economic or market-based instruments (MBIs) – such as indirect taxation, target subsidies or tradable emission rights, given that they provide a flexible and cost-effective means for reaching given policy objectives.

CONTENT: the purpose of this Commission paper is to launch a discussion on advancing the use of market-based instruments or MBI's in the Community. Under scrutiny are energy use, the environmental impact of transport on the environment, the sustainable management of water, waste management, protecting Europe's biodiversity and reducing air pollution. Particular attention is given to the Energy Taxation Directive.

Using market-based instruments for Community policy purposes: MBI's carry certain advantages over and above other regulatory instruments. For example:

- They improve price signals, by given a value to the external costs and benefits of economic activities, so that economic actors take them into account and change their behaviour to reduce negative environmental impacts.
- They allow industry greater flexibility in meeting objectives and thus lower overall compliance costs.
- They give firms an incentive (in the longer term) to pursue technological innovation and to further reduce adverse impacts on the environment ("dynamic efficiency").
- They support employment when used in the context of environmental tax or fiscal reform.

In addition, they have proven useful in terms of preventing any distortion of the EU's internal market. MBI's have lead to a number of EU initiatives including the EU Emission Trading Scheme, the Energy Taxation Directive and, in the field of transport, the Eurovignette Directive.

The EU is strongly committed towards ensuring environmentally sustainable developments as well as promoting the Growth and Jobs agenda. An environmental tax reform (ETR) could shift the tax burden from welfare negative taxes (e.g. on labour) to welfare positive taxes (e.g. on environmentally damaging activities such as resources use or pollution). As well as discouraging environmentally damaging behaviour through taxation, Member States may also use fiscal incentives such as subsidies to encourage green behaviour, facilitate innovation, research and development.

The paper recognises the right of the Member States to find the correct balance between incentives and incentives in their tax systems. It points out, however, that a Community fiscal policy will be able to facilitate the right balance between fiscal constraints and fiscal neutrality. In terms of environmentally harmful subsidies the paper questions what the best way may be to advance the process of reforming environmentally harmful subsidies.

Options for applying MBI's to influence energy use: Energy is currently top of the EU priorities given that it represents a major challenge in terms of sustainability, security of supply and competitiveness. The paper recognises that current EU legislation has been designed to serve primarily the internal market. However, the Community Energy Taxation Directive could also serve to play a more useful role in terms of environmental sustainability. Energy taxation potentially offers the EU the chance to combine the incentive role of taxation in favour of more energy-efficiency and environment-friendly energy consumption, with the ability to generate revenue. As it currently stands, the Energy Taxation Directive is unable to fulfil such ambitions. The paper suggest that one future option might be to divide the Community minimum levels of taxation into energy and environmental elements (or counterparts), which would be mirrored at national level in the form of an energy tax and an environmental emissions tax. This would build on the existing approach in energy taxation but would make it more coherent, while refining its environmental aspects.

Of the different Community market-based instruments existing in the field of energy, transport and environment, energy taxation is considered the most cross-cutting, with impacts in all three areas and directly interacting with all other instruments. Yet, the current European Emissions Trading Scheme (ETS) applies to certain combustion and industrial installations only – while energy taxation applies to fuel uses of energy only. This means that a number of the most energy intensive sectors are outside the scope of the Energy Taxation Directive. The Commission, therefore, questions whether certain sectors already covered by the EU ETS could be excluded from the scope of the Energy Taxation Directive to the extent that their greenhouse gas impact is adequately addressed by the EU ETS.

Options for the further use of MBI’s in environment policy: Transport is a major contributor to air pollution and CO2 emissions. This trend is increasing. For example, in 2004, transport alone was responsible fore 22% of total CO2 emissions, aviation and shipping accounting for a further 3-4% of total GHG emission. Proportionally speaking, aviation emissions have grown rapidly since 1990. Several initiatives have been adopted in order to tackle transport emissions. For example, the proposed introduction of a CO2-dependent element in the tax base of both annual circulation and registration taxes in the Commission’s proposal for passenger car related tax. Other initiatives have included the Eurovignette Directive, which provides a charging framework on trans-European road networks.

Conclusion: The Commission concludes by stating that alongside regulation and other instruments MBI’s should be used as a cost-effective tool to achieve environmental and other policy objectives.

By means of this paper, the Commission hopes to generate a discussion on the Community’s contribution to market-based instruments and the role of indirect taxation in particular. The paper also identifies further areas for the application of MBI’s – ones that could advance best practice. The Commission is now seeking reactions to the ideas and specific questions that have been raised in the paper as well as comments on the type of MBI to be chosen. Replies should be sent to the Commission by 31 July 2007.