Ecological Tax Reform in Denmark: history and social acceptability

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Abstract

Despite the long-term and positive experience with Ecological Tax Reform (ETR), the PETRAS study indicates that awareness about the principles behind ETR is low among both businesses and the general public in Denmark. As well as the lack of awareness of ETR, attitudes towards environmental taxation appear negative. When explaining the political intentions behind ETR, attitudes seem to improve somewhat, but they still remain overall sceptical.

Based on the history and the results of the PETRAS project the article will describe some of the main impediments for further development of environmental tax and ETR policies in Denmark. The article concludes that the main reason why the ETR policy has been met with such apparently low social acceptability in Denmark is that the "green" of the "green" tax reform has been somewhat oversold. On this basis it recommends the pursuit of a courageous government strategy of, openly and repeatedly, stressing the revenue purposes of environmentally related taxes over the environmental purposes in an effort to redirect public discussions towards relevant issues like the pros and cons of environmentally related taxation compared with other types of taxation and the connection between the overall tax burden and demands for government spending. Such a bold government "confession" to the obvious revenue purposes of the environmentally related taxes could make them, if not popular, then at least a bit more acceptable to businesses and the general public.

1. Introduction

Denmark can be seen as part of a “first wave” of countries to move towards a comprehensive use of environmental taxes and Ecological Tax Reform (ETR) in the late 1980s and early 1990s, responding to an, at that time, relatively strong popular demand for increased and more effective environmental regulation.

This article will start out by providing a short historical introduction to the ideas of environmental taxation and ETR. This will be followed by a historical outline of the development of environmental tax and ETR policies in Denmark, stressing some of the main drivers and impediments involved. The historical account is among other things based on interviews with key policy makers (Klok, 2002; Pedersen, 2003).

Following the historical accounts the article will report the results of the Danish PETRAS study of business and public awareness and attitudes towards ETR that was carried out in 2001. The aim of PETRAS was to examine the knowledge and attitudes of businesses and the general public towards policies of ETR. The examination has been based on interviews with representatives from five different companies and with five focus groups comprising of members of the general public.

Based on the historical account and the PETRAS results the article will observe some of the main impediments for a further development of environmental tax and ETR policies in Denmark. The article concludes that the main reason why the ETR policy is
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2. Historical background

2.1. Environmental taxation and ETR

Environmental taxation has been discussed, and in some cases implemented, since the early 1970s. At that time the OECD defined and recommended the principle that the “polluter pays”, according to which the polluter should bear the expenses of carrying out the measures laid down by public authorities to ensure that the environment is in an acceptable state (OECD, 1972). But it was not until the 1980s and early 1990s that the concept of environmental taxation got its first serious international breakthrough.

Inspired by the classical welfare economic theories of Pigou, a number of American and British environmental economic studies started in the late 1980s to describe environmental taxation less as a way to make “polluters pay” for environmental cleanup or protection measures, but more as a possibly more efficient, economic or “market-based” instrument for environmental regulation. This was in comparison to traditional bureaucratic “command and control” methods (Baumol and Oates, 1988; Pearce et al., 1989). Environmental taxation would make the price of polluting activities reflect the true social costs involved, while providing agents with effective economic incentives to reduce levels of environmentally harmful consumption or effluents. Besides the provision of more value for public money spent on environmental protection measures, environmental economists later added a “double dividend” as a possible additional benefit to be derived from environmental taxation. The view was that while most taxes distort incentives, environmental taxes correct distortions, namely the externalities arising from the excessive use of environmental services. If the revenues from environmental taxes were used to finance reductions in other incentive-distorting types of taxation, such as labour supply, investment or consumption, secondary gains could be created in addition to the environmental benefit (Oates, 1991; Helm and Pearce, 1991; Smith 1992). The new ideas of environmental economics have later been supported by the OECD, stressing that environmental taxation can be effective in terms of environmental protection, when properly designed and implemented, and that environmentally related taxes can contribute to the integration of environmental and economic policies (OECD, 1989, 1993, 1997; European Commission 1993).

Finding their basis in conventional mainstream economics, environmental economists have been careful to stress the need to base environmental action on the proper valuation of environmental goods in order to enable a clear assessment of both the costs and benefits of environmental action. While environmental economics in this way promised to strengthen the possible regulatory measures derived, it could just as easily be used to stress the many uncertainties still involved, and thus to justify delays in regulatory action. In this regard, environmental economics has, for example, been careful to stress the international or global nature of many modern environmental problems, and thus how taxes imposed in one country might only contribute small amounts to overall emission reductions, while hurting the international competitiveness of national businesses. Furthermore, some economic studies in recent years have begun to question the wisdom of the “double dividend” theory, stressing the uncertainty of the secondary gains and how these might easily be outweighed by the adverse economic effects involved with excessive environmental taxation (Bye, 2002; Goulder 1995).

The careful pragmatic approach of mainstream environmental economics has all along found a more political ideological counterpart in the concept of “ecological modernism”. This concept can be traced to some innovative ideas on the correlation between environmental protection and economic growth presented in the debate of the mid-1980s in Germany. Rejecting the conventional wisdom that environmental protection had to be a threat to industrial competitiveness and employment, ecological modernism predicted that the environmental challenge could in fact stimulate economic growth similar to the “Wirtschaftswunder” or “economic miracle” that Germany had experienced in the 1950s and 1960s. Properly designed, increased environmental protection would create new “green” jobs and spur technological innovation. In this regard economic instruments, such as taxation, were shown to provide the most powerful means of regulating pollution in a market economy, ensuring economic efficiency and forcing the development of cleaner technologies (Wicke, 1986; Andersen, 1994). The social economic policy of Ecological Tax Reform (ETR) can also to be associated with German “ecological modernisation”. In 1983, a proposal to raise the taxation of all non-renewable forms of energy by 3.5% annually over a 10-year period received wide attention in Germany. The basic idea was that if revenues from this tax increase were used to finance workers’ pension funds, thereby relieving the social costs to employers, the overall result would be increased employment with less environmental degradation (Binswanger et al., 1979, 1983). The concept of ETR was later refined, by adding forced technological innovation (and thereby improved competitiveness on growing international markets for clean technologies) to the list of benefits promised. All economic sectors,
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