

# Social and political responses to ecological tax reform in Europe: an introduction to the special issue

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## Abstract

This paper introduces the special issue on the Policies for Ecological Tax Reform: Assessment of Social Responses (PETRAS) project about responses to ecological tax reform (ETR) in Europe. Although ETR is widely accepted to be a policy with desirable effects, its implementation has been limited by problems of political acceptability. The project aimed to address the question of how to make such a policy more acceptable. It is the first study to examine in depth the thinking of members of the general public about the ETR policies and is also the first international comparative study of the thinking of ordinary business people about ETR policies. The PETRAS project methodology was based around the use of interviews and focus groups to inform the assessment of social responses to ETR policies and the development of improved designs for them. A number of issues emerged relating to awareness, trust, understanding of the purpose, visibility, incentives, regressivity, levels of taxation, terminology, communication about ETR and the use of alternative instruments. Together with these similarities, a pattern of differences between the countries can also be seen. The final section of this paper introduces the national studies described in the following papers.

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## 1. Introduction

This special issue is devoted to the results of a recent European Commission Framework 5 project on responses to ecological tax reform (ETR).<sup>1</sup> The research examined the attitudes of policy makers, businesspeople and the general public towards in ETR policies in five European Union (EU) member states (Denmark, France, Germany, Ireland and the UK) selected to represent countries at different stages in the debate about ETR. This paper serves to introduce the project and the issues it addressed. It is followed by papers from four of the participating countries in turn, describing the

research conducted in each of them in more detail. The final paper deals with the wider implications of designing a tax system based on the political ramifications of the results.

Ecological tax reform and environmental tax reform are two terms that are used interchangeably. ETR increases taxes on natural resource use, use of polluting products or pollution and lowers other taxes, usually those on employment. The rationale is that the tax burden should fall more on ‘bads’ than ‘goods’ (which is not currently the case), such that appropriate signals are given to consumers and producers. The move towards a more appropriate tax base having appropriate signals, can lead to a ‘double dividend’. The ‘double dividend’ argument is that higher taxes on energy will lower energy use and hence pollution, while lower taxes on labour will reduce pressure on employment and contribute to decreasing unemployment. There are

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<sup>1</sup>‘Policies for Ecological Tax Reform: Assessment of Social Responses’ (PETRAS), Contract Number EVG1-CT-1999-0004.

variants on ETR that would instead return the money raised in other ways. The environmental fiscal reform (EFR) is a broader term encompassing the removal of subsidies.

The PETRAS research is the first to examine the responses of members of the general public and ordinary businesspeople to ETR policies and proposals. ETR can be applied to many activities, but the most common among European countries to date has been taxes on carbon emissions or energy use. PETRAS examined policies and proposals applying to these.

Although ETR is widely accepted to be a policy with desirable environmental, economic, and employment effects, its implementation has been limited by problems with political acceptability.

The purpose of the research was to develop proposals to improve the design of ETR policies in Europe in order to maximise their political acceptability while still attempting to meet the environmental, economic and employment objectives behind ETR. The six specific objectives were:

- (1) to assess the patterns of awareness of ETR policies;
- (2) to gauge the understanding of the intentions behind ETR in terms of environment and employment;
- (3) to assess patterns of support or opposition towards specific policies and the general principles of ETR;
- (4) to identify specific objections to these policies and principles;
- (5) to assess what sort of ETR design would be regarded most favourably;
- (6) to assess how far that design might compromise the effectiveness in meeting environmental, economic and employment objectives.

## 2. Background

The EU has encouraged the use of market-based instruments both across the Union and in member states. The Environmental Action Programmes of the EU outline the European Commission's intentions and recommendations regarding environmental policy. Ultimately these Programmes are translated into Regulations, Directives, Recommendations and non-binding Opinions (Artis and Lee, 1997). Directives, the most common instruments of EU Environmental Policy, are binding as to the results but not the method of achieving them. The sixth environmental action programme, covering 2001–2010, which outlines the main environmental-policy issues facing the EU and the policy instruments available, emphasises the integration of the economy and the environment. It places emphasis on the use of economic instruments.

The rationale for the application of economic instruments is that the internalisation of externalities corrects markets and distorted prices, provides room to cut more distorting taxes thus improving the overall effectiveness of the fiscal system and reinforces other instruments, in particular regulation, characterised by enforcement deficits. At the microlevel of businesses and individual decision makers, the choice to improve or pay for pollution is left open, incentives for improvements in efficiency are continuously provided, innovation is spurred and guided, and diffuse pollution sources are addressed.

Of all the economic instruments, environmental taxes and charges are the most frequently used economic instruments (Clinch and Gooch, 2001). However, this may be set to change with the new Directive on Emissions Trading (European Community, 2003). The Commission may be redirecting their efforts in this direction as the unanimity rule, which has held up environmental taxation since its inception, does not apply. Taxes and charges impose an obligation on users to pay for the use of the environmental resources. These bring the costs of pollution and of using environmental resources into the prices of goods and services produced by economic activities. Emissions and effluent charges and taxes are levied upon the quantity and/or quality of discharge into the air, water and soil, and are based either on direct measurement or estimations of discharge. Product charges and taxes are levied on products that cause environmental damage through their extraction, production, use and disposal (Danish Environmental Protection Agency, 1999). They may take the form of a charge or tax relating to the composition of the product, e.g. the phosphorous content of fertilisers or they can be levied upon the product itself, e.g. a fuel tax (OECD, 1994, p19). Resource-use charges are payments made in return for direct use of an environmental good. Payments may be implemented on the basis of quantity (e.g., mining tax), time scales (e.g., hunting and fishing permits) or access (e.g., national park entrance charge). User charges are payments made in return for the provision of a service, such as the collection and treatment of emissions and waste, for example, sewage charges and municipal waste charges.

Taxes and charges are revenue raising and there are several options to recycle revenues as outlined by Baranzini et al. (2000):

- 'Tax reform' (or revenue neutrality) whereby revenues from an environmental tax are used to decrease other taxes, so that the government budgetary position is unchanged and the overall tax burden remains the same. The general underlying principle is to shift taxation from economic 'goods' (like work, income or property) to environmental 'bads' (like pollution).

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