





#### **Environmental Fiscal Reform**

## A Practice-Orientated Training for Policy Makers, Administration Officials, Consultants and NGO Representatives

commissioned by









# **Environmental Fiscal Reform (EFR) Concepts and Definitions**

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#### **ETR** definition

Environmental tax reform (ETR) can be defined as a reform of a national tax system which may include increased taxation of environmentally damaging products/activities, and/or use of natural resources. This is sometimes combined with a reduction of the tax burden on economic 'goods' such as labor, investment and/or sustainable consumption. As a result, the tax burden is shifted towards economic 'bads' and away from economic 'goods'. Important incentives are provided to gradually steer the economy towards more sustainable for Economic Cooperation and Development consumption & production and green growth.







#### **EFR** definition

Environmental fiscal reform (EFR) includes ETR but can be characterized as a broader approach, which focuses not only on reforming/greening the tax system, but also on reforming public environmental expenditure and/or reforming economically motivated subsidies, which counteract environmental policy. Additional ways of greening fiscal policies may be included in EFR strategies too.

Source: Adapted from European Environment Agency







### Rationale and justification of an EFR (1/2)

- Most environmental assets are public goods which have an obvious value but are not exchanged on markets (e.g., clean air, clean water, fishery resources, ecosystems, etc.), and therefore no price emerges to signal scarcity. EFR assigns such price reflecting scarcity.
- Economic activities generate pollution and waste that leads to costs to others 'externalities' (e.g., increased health costs due to air pollution related respiratory diseases). ETR/EFR helps internalize' such 'external' costs.

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#### Rationale and justification of an EFR (2/2)

- By providing appropriate price signals, EFR encourages a more efficient allocation and use of natural resources.
- EFR allows for a more cost efficient implementation of environmental policy.
- If designed properly, EFR may generate significant economic value added and trigger the creation of new jobs facilitating green growth.





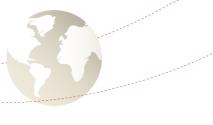




### EFR policy instruments (1/3)

- <u>Tax shift</u>: taxing 'bads' rather than 'goods'
- Environmental taxes and charges, levied for example on air emissions (CO2, SO2, etc.), water effluent/pollutants, water abstraction, energy sources, transport (taxes on circulation, vehicle registration/ import/ emission, motor size, etc.), landfill and/or incineration, natural resources (raw materials, minerals, etc.), environmentally harmful waste products (packaging, electronics, tires, pesticides, batteries, used chemicals) etc.;
- Other fiscal instruments such as import duty differentiation, VAT rate differentiation, accelerated depreciation, etc.;
- <u>Emissions trading</u> which can help ensure that a given overall emission target is met via the allocation and trading of emission allowances;









## EFR policy instruments (2/3)

- Green subsidies, such as grants, soft loans, interest rate subsidies, loan guarantees, equity etc. for investment that catalyzes/enables the implementation of environmental or green growth policies and for catalyzing/enabling the uptake or mainstreaming of environmental technologies;
- Reform of environmentally harmful subsides, e.g. subsidies that were introduced for other purposes than environmental policy but effectively counter-act environmental policy or support unsound environmental practices;
- Green public procurement which catalyzes the mainstreaming of environmentally sound technologies and fosters the environmental industry by implementing sustainability criteria in purchasing decisions;

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### EFR policy instruments (3/3)

- Measures aimed at <u>"greening" the yearly or longer term</u> <u>public budgeting processes</u>, e.g., by systematically implementing sustainability criteria in budget formulation and implementation;
- Measures aimed at <u>greening commercial finance</u> (e.g., green financial products and services offered by commercial banks, insurance and leasing companies);
- Measures aimed at greening FDI, greening ODA, greening public private partnerships, green public-private voluntary agreements, etc. may also be included in EFR solutions/packages.









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