Carbon and Energy Tax Reform in Europe (CETRiE)

A PARTNERSHIP BETWEEN GREEN BUDGET EUROPE AND THE EUROPEAN CLIMATE FOUNDATION
IN ASSOCIATION WITH VIVID ECONOMICS

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To
EU Ministers of Finance

Dear Minister of Finance,

We – Prime Ministers, former Ministers of Finance, current and former political decision makers – are writing to you ahead of the Council Meeting on 15 May 2012 and the European GDP report from Eurostat urging you to implement new innovative political solutions and to contribute to the required fiscal consolidation with the least economic impact.

We ask you to consider the findings of a major new study that is published today on carbon and energy tax and pricing reforms in Europe.

After almost four years of the most serious financial and economic crisis Europe has seen in 80 years, most Member States of the European Union are facing substantial annual budget deficits and are struggling with high public debts. Most of the EU Member States have agreed on ambitious austerity measures. However, we all know that this is not a sustainable alternative to the fundamental and sustainable reform of our economies. The growth compact recently discussed will only be a success if it is nourished by robust knowledge and innovative ideas.

Cut the deficit, cut carbon - the win-win of smart energy taxes

Governments across Europe and the world are in a Catch-22 situation when it comes to tax. National debt is a mill-stone round the neck of every European economy and governments need to raise revenue to pay off debt and reduce deficits. At the same time, they are looking to consumers to start spending, to kick-start growth and get money flowing round the economy once more. One answer to this dilemma has been austerity and the debate is now moving towards measures that will stimulate growth rather than just reduce spending. Smarter taxation will be vital to getting the balance right.

When governments think about the difficult task of raising taxes, they usually think about income tax, business taxes and VAT. But there are other taxes which can also raise significant amounts of revenue with much less damaging impacts on the economy. These are the taxes governments already levy on energy and carbon use in transport, and on electricity, coal and gas. Such taxes already play a crucial role in cutting the emissions which cause climate change. But recent research shows that they can also play a useful role in raising government revenue whilst minimising impact on economic growth.

Pound for Pound, Euro for Euro, energy and carbon taxes have a lower negative impact on the economy, consumption and jobs than income tax and VAT. For example, raising direct taxes can reduce consumption by twice as much as energy and carbon taxes raising the same revenue. Maintaining consumption at as high a level as possible is vital, it frees money for consumers to spend and boost the economy. Carbon and energy taxes can raise revenue while leaving the economy is a stronger state to sustain the recovery. Conventional taxes raise revenue, but pose a much greater risk of depressing growth in the process.

This is not the only reason why looking more closely at carbon-energy taxes makes sense. The current picture of energy taxation in Europe is not sustainable. Tax rates on different fuels vary by over 50% across the EU. The costs of doing business and the wildly differing incentives resulting from fuel costs cause major distortions in the European single market. Creating a level playing field in the EU on energy taxation will reduce tank tourism, help all our economies and our climate.

Rising energy bills are however a massive political issue in many European countries. Driven by the cost of fossil fuels, consumer energy prices are rising everywhere. Energy taxation however tends to produce a benefit for consumers overall when judged against other forms of taxation. The economic benefits of avoiding the negative impacts of conventional taxes work across the economy, benefitting the least well-off across their household budget and in terms of their expendable income.

Most energy and carbon taxes are levied by national governments. But another option for raising revenues is the European Emissions Trading Scheme. In terms of the effect on GDP and jobs, the macroeconomic costs of raising this revenue would be less than the costs of raising the same amount by income taxes or VAT – potentially by as much as a third. In the context of Europe's fiscal deficits and the economic impact of dealing with them, that is a huge potential prize if the issues depressing the carbon price can be addressed. Taking the massive over allocation of pollution permits out of the system will be vital.

So as European Finance Ministers meet today in Brussels, they should be thinking more imaginatively about their fiscal options than they have done in the past. Carbon and energy taxes can produce better economic results than conventional taxes, as well as helping to cut emissions. They offer less pain, and more gain. Europe needs a fiscal recovery, its needs to cut its emissions and it needs a strategy for growth. Carbon taxes and an effective ETS can be a powerful part of the solution.

Less pain, more gain: carbon-energy pricing, nationally and EU-wide, is worthy of serious consideration in the mix of revenue raising strategies.

Finance ministers should think hard about fiscal, social and environmental sustainability when formulating policies to bring about a recovery.

In view of the public interest in this matter, we intend to make the contents of this letter more widely available. Thank you for your attention to the matters raised in this letter.

Yours sincerely,

Hans Eichel, former Minister of Finance, Germany, 1999-2005

Yannis Palaiokrassas, former Minister of Finance, Greece, and European Commissioner for the Environment and Fisheries

Dr. Josef Riegler, former Vice-Chancellor, Austria

Dr. Martin Bursík, former deputy Prime Minister, former Environment Minister, Czech Republic

Dr. Franz Fischler, former EU-Commissioner for Agriculture and Fisheries