

44 – 100 Years of Externalities

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A hundred years after Arthur C. Pigou's call to put price on externalities, a number of different theoretical and methodological approaches to internalisation of external costs later, the polluter pays principle has still not resulted in a real change of price signals.

In the European Union (EU), competences in the taxation field generally remain with Member States. Taxation is the last EU policy area where decision-making relies on unanimity, which makes EU level coordination a lengthy and not always successful process. To date, EU tax policies have mainly focussed on targeted deliverables responding to specific problems. There is no common and holistic vision for EU tax policies that is shared by all Member States. Coordination is even harder when we move to the global level.

With the Covid-19 crisis, tax revenues have come under immense pressure. Part of our response to the crisis needs to look at taxation in a systemic and structural way. Future-proof tax systems needs to address current and emerging challenges brought by not only the Covid-19 crisis, climate change and environmental degradation, but also by globalisation, digitalisation and ageing of population. These challenges need to be addressed through systemic reforms rather than a piece meal approach addressing different issues in isolation. Such reform(s) need to take into consideration the need to ensure sustainability of tax revenues, support the transition to a green economy, ensure social justice for citizens and competitiveness for business. Shifting taxation from labour and business to unsustainable consumption and pollution has a potential to address all these aspects, in particular if coordinated at EU and international level.

Countries should step up their effort in putting prices on externalities with due regard to adverse social impacts. In the EU, the already announced revision of the Energy Taxation Directive and ETS and introduction of a Carbon Border Adjustment mechanism could be important elements introduced in a context of broader tax reforms for which the European Green Deal calls.

It is in the strong interest of Europe to support and cooperate with our international partners on also taking forward the necessary sustainable fiscal reforms outside Europe. There is popular perception that the regressive effects make environmental taxes undesirable despite their environmental benefits. Despite the perception of regressivity, if properly designed, the effect of reforms on the poor can be offset by using the revenue for redistributive expenditure, similar to other taxes.

Biographical note

Astrid Ladefoged is Head of Unit for Sustainable Development Goals, Green Finances & Economic Analysis within DG Environment at the European Commission. Her unit works on developing environmental strategy through the implementation of the European Green Deal and through better regulation and economic analysis. The unit promotes implementation of the UN Sustainable Development Goals and ensures co-ordination of environmental issues in G7/G20 and OECD processes. It drives the integration of environment and resource efficiency considerations into EU policies and the promotion of market based instruments. It contributes to the promotion of green jobs and skills and greening the financial system. Astrid has more than 20 years of professional experience with the EU's green policies including at national level in a ministry, at European level in a think-tank and finally for more than 15 years in the European Commission in several departments and in the cabinet of former Commissioner Vella.