SUBMISSION BY THE SOCIETY FOR THE ENVIRONMENT TO THE EAC INQUIRY INTO HM TREASURY AND SUSTAINABLITY FEBRUARY 2016

Summary

The Society provides commentary on green growth and economy to provide a background for the Committee's deliberations. In doing so it makes a number of suggestions:

- We suggest that the opportunity should be taken for a radical rethink of environmental taxes; an inspection of what is included now suggests a reflection of a collection of historical and separate initiatives rather than a consistent approach.
- Some natural resources are paid for in different ways such as abstraction charges for water which are paid to the appropriate regulators. We suggest a broader integrated approach and instead a natural resources or future generations tax and incentive framework, which has the twin objectives of behavioural change and paying to use resources.
- The ambiguity of there being environmental elements in general taxes should be clarified and should have a clear natural resources element as a subset including a good understanding of how natural resources research and development is included in tax allowances.
- There should be clear articulation of hypothecation. This change should be about better focussing management of resources, mitigating environmental harm and improving the environment without rendering the UK less competitive.

Context

The Society welcomes the opportunity to comment on the relationship between fiscal, economic and environmental matters. It focuses more on the last question posed by the committee on green growth and in doing so it hopes that it will provide some insight into answers to the other questions.

There are many concepts underpinning green growth. We are not convinced that there is clarity around the understanding of the meaning of some phrases and the concepts behind them and how they all fit together. Examples include:

- Sustainability
- Green economy, growth, finance, bonds investment, infrastructure, incentives
- Environmental incentives
- Environmental taxes
- Low carbon economy
- Natural capital management
- Natural resources management
- Paid ecosystems market
- Crowd funding

Green Growth

Green growth is about fostering economic growth, development and social inclusion while ensuring that the natural assets provide the resources and environmental services on which our well-being relies. To do this, Government must stimulate investment and innovation to underpin sustained growth and give rise to new economic opportunities, human capital formation and skills building, and redistribute the proceeds of growth.

We refer to categories of green growth recommended by the OECD in 2010. The notion of integrated natural resources management fills the same intellectual space as natural capital. There is also the common notion of excessive growth (along with excessive pollution) and this is sometimes expressed as 'multi-planet living'. We suggest that green growth is the mechanism by which a green economy grows. This leads to some challenging dilemmas, which if resolved, will provide some clarity. Does an economy grow in terms of its total value whilst remaining at some state of greenness or does an economy remain static whilst becoming greener? This is a manifestation of the growth or no growth debate on the future of economies. Or is it a bit of both? Is there an absolute yes/no state of affairs which defines a green economy - if the answer is no - then the mixed option is that an economy seeks to grow and at the same time metamorphose to be greener? So understanding what constitutes a green economy and how to measure it is an essential context for understanding where the Government wishes to travel and begins to bring the pieces of the jigsaw together.

Green Economy

The best definition for a Green Economy is from UNEP who define a green economy as '*an economy that results in reducing environmental risks and ecological scarcities, and that aims for sustainable development without degrading the environment*'.

It is closely related with ecological economics, but has a more politically applied focus. The 2011 UNEP 'Towards a Green Economy' report argues "that to be green, an economy must not only be efficient, but also fair". Fairness implies recognising global and country level equity dimensions, particularly in assuring a just transition to an economy that is low-carbon, resource efficient and socially inclusive.

The debate we hear and see in the papers and in politics is whether becoming 'more green' reduces competitiveness in world markets for an economy or, whether it provides more opportunities to grow national income. The ultimate in the greenness scale is 'One Planet Living '. No country has achieved this yet, but on the other hand no country has been deemed to be not green at all. Interestingly some countries have do not have particularly green economies, but flourish because the economy is small compared to locally available natural resources reserves.

So to articulate the relationships, the goal is to achieve the desired state of a green economy, however it is structured. This is achieved by green growth, which is facilitated by

green investments and green finance particularly in green infrastructure. The mechanisms of finance can include instruments such as green bonds, crowd sourcing and paid ecosystems markets. Natural capital and natural resources management are mechanisms which bring together the concepts of environmental and economic management in a practical way. In Wales this purpose underpins the work of Natural Resources Wales and the recent proposal that a new duty be given to environmental regulators in England. The Society very much supports this important concept and agrees with the Chancellor's autumn 2015 Budget statement 'going green should not cost the earth'.

What is the structure of a Green Economy? In the simplest terms it may be divided into economic activity from the exploitation of natural resources, perhaps defined as that arising from natural capital through ecosystem services, and economic activity from all other sectors All sectors should create value whilst not creating excessive cost - this is the basic concept of added value. All will have some sort of impact but it is not straightforward that green sector industries are necessarily deep green in colour and vice versa.

So in extremis, it would be possible for a green sector industry like commercial fishing, including processing, to have high environmental impact by overfishing and irresponsible disposal of processing wastes, but for non-green sector manufacturing of high tech white goods to be environmentally responsible and carbon neutral. It must be recognised that all sectors contribute. There is a need for effort to ensure that good environmental practice is used by all sectors, for example by eradicating irresponsible waste management. No sector should be excluded. There needs to be consideration on how taxes and incentives work normal to encourage all economic growth and a circular economy in a sustainable way.

An economy has momentum, and infrastructure has replacement inertia. So for example it takes a long time to replace power generation assets. The challenge again is that commentators tend to focus on response to climate change and reliance on renewable energy as the central definition of a green economy. In our view a green economy can include all industries, if they are managed sustainably, but it has a massive challenge in becoming a deep green economy in the global competitive sense because of the central driver of renewable energy in the definition. An understanding of the total and exploitable natural resources of kinetic, potential, gravitational and radiant energy of the UK through wind turbines, solar arrays, hydropower, tidal power and so on will be key to increasing the green hue of the Country's economy and must be supported.

There are other elements in the ecological footprint of a Country other than carbon. This includes, for example, the impact on the state of nature, and of the need to move forward with a harmonious balance of the needs to improve the economy and the state of nature mechanisms in place particularly through the ways in which planning works. It is about nature conservation being at the heart of flourishing natural capital. The same is true for societal wellbeing.

Regulators of natural resources should ensure that advice always converges on green growth towards a very green economy. Equally they must contribute by ensuring that in

their roles as regulators, they are focussed on the same goals. So once everyone is complying with consents and licences, there is a good platform to start thinking of the economy as being quite green. That requires 'fit for purpose' consents and licences monitored sensibly and using the full force of law against abuses. These 'fit for purpose' consents etc, must be based on sound legislation, strategies and policies.

The Society suggests that there needs to be a national consensus on what we mean by a UK green economy and how we are going to manage it. We do not have space to elaborate the systems available to measure how green the economy is, but we commend a development of the Dual Citizen model, to which the UK contributes already, and we would be pleased to share further information with the Committee.

Green finance

The Society is pleased that the financial markets are mobilising to provide the necessary support to develop green infrastructure and that standards will determine the robustness of these services. However, the Society is concerned that caution has to be exercised in trading of any instruments so as to avoid the past mistakes of derivatives trading. It therefore considers that the financial regulators must play a strong role.

Green taxes and incentives

The previous Government published its definition of environmental taxes in 2012. The definition was designed to encourage effective policy making, and also measurement of progress against its pledge to increase the proportion of revenue that comes from environmental tax.

Environmental taxes are defined as those which meet all of the following three principles:

- *the tax is explicitly linked to the government's environmental objectives;*
- *the primary objective of the tax is to encourage environmentally positive behaviour change; and*
- *the tax is structured in relation to environmental objectives, for example: the more polluting the behaviour, the greater the tax levied*

Applying these principles, the Treasury has identified the following taxes as environmental, and these will comprise the baseline against which the government's commitment to increase the proportion of environmental tax revenue will be measured.

The Office of Budget Responsibility forecasted that the proportion of revenue from these taxes would double by 2015-16.

- Climate Change Levy
- Aggregates Levy
- Landfill Tax
- EU Emissions Trading System (EU ETS)

- Carbon Reduction Commitment Energy Efficiency Scheme (replaced in 2015 by Capital allowances on energy efficient items)
- Carbon Price Support

The Government saw this as an important step in meeting its commitments on environmental tax, and the broader determination to be the greenest government ever. Indeed, through policies such as the Carbon Price Floor, the Government foresaw that it would double the proportion of environmental tax revenue by the end of the Parliament (the current Government has pulled back from this objective). In 2012 the OBR predicted that environmental taxes would rise from 2.5B£ out of 551B£ total tax (0.5%) in 2010/11, to 6.1B£ out of 660B£ (0.9%) in 2014/5 and to 6.6B£ out of 692B£ in 20156 (1.0%). However the ONS reported in 2014 that environmental taxes raised £44.6 billion in the UK in 2014.

- Despite rising by an average of 5.0% per year since 1993 (in current prices), environmental tax revenue has remained broadly stable as a percentage of GDP (2.5% in 2014).
- Environmental taxes provided 7.5% of all revenue from taxes and social contributions in 2014.
- Hydrocarbon oil duties (including transport fuels) accounted for 60.8% of all environmental taxes in 2014.
- Households paid an average of £765 in environmental taxes in 2012.

So in our view there is still some opacity in the description of what is an environmental tax and agree with the views of the Treasury Select Committee expressed this month.

We are aware of the dismay over the announced changes in the Summer 2015 Budget to the Climate Change Levy (CCL), From August 2015, the Government removed the exemption that businesses currently enjoy from the CCL for sourcing renewable energy. We do not wish to make an extended submission on renewable energy, but we are dismayed at the mixed reaction over the impact of the Autumn Statement. Whether or not more renewable energy is used is dependent on many factors beyond simple taxation, such as the role of DECC and the energy regulators on matters such as contract for difference auctions, capacity payments, feed in tariffs, but most particularly, the commodity market prices of fossil fuel. These are subject to geopolitical factors which make forward planning very difficult.

The Society supports all efforts to take a longer term view, that to follow what is needed in absolute scientific terms and to honour the international commitments such as the Paris Agreement; recognising that burning what remains of fossil fuels, may undermine emissions targets, in addition to the fact that they are a diminishing and progressively more expensive resource. Therefore, steps have to be taken now to increase the support given to renewable energy. We have to set aside the immediate issues of the continuing availability of cheap fossil fuels and prepare for the future. We are not convinced that that Autumn Statement will help with this long term approach, although we commend the increase in the

investment in research. As is often said, and emphasised by the Chancellor in the Autumn Statement, more long term investments in infrastructure are needed. There does need to be a better balance between dealing with the immediate problems of the present and with those of a long term uncertain future. The current debates on investments in flood risk management highlight this.

There is, however, a dilemma in all of this. Whilst the Society is not an expert taxation body, it would seem to us logical to see environmental taxes in the context of three categories

- First, as the Government describes them, they are a mechanism to change behaviour, and in that context the long optimistic expectation is that the revenue will fall as behaviours change; decisions have to made about the fate of the revenue whilst it is being raised. It makes sense that this should be hypothecated for an environmental purpose. For example, into building the skills capacity needed to meet the demands of an emerging green economy;
- second, as a user tax for the exploitation of natural resources, which would have a long term horizon, if the resources are used sustainably; and
- third, whereby they are subsumed into a broader tax, such as s Vehicle Excise, Fuel and Air Passenger Duties. These will not be hypothecated unless it is treated as a separate tax collected alongside the more general tax.

This is an elaboration of the Treasury definition since pollution should be regulated sustainably first and not bought. We agree with the report 'Natural Partners' published by the Green Alliance. The use of natural capital accounting does not justify any retreat from environmental regulation. In a report comparing traditional conservation and newer natural capital approaches, published on 25 January, the think-tank says there will be a continued need for a regulatory framework for nature as environmental threats to it rise.

The Government wants a clear approach that delivers a positive environmental impact without adding burdens onto business or households. The Society is aware of the demands of austerity but also recognises these as the 'mother of innovation' but it also recognises the difficult choices which have to be made in the competing demands on public finance. It is also aware of the potential burden which taxes may add to the costs of goods and services thus reducing competiveness, so we would urge all decisions on these matters to be based on the concept of 'impact on goods and services to customers'… just how much does a tax cost the ultimate customer and in itself reduce competiveness? Perceptions should be based on objective data rather than subjective opinion.

The Government will also continue to explore opportunities to further green the tax system through the course of the Parliament in a way that is consistent with the aims of tax simplification and deficit reduction. The Society suggests that the opportunity should be taken for a radical rethink of environmental taxes; an inspection of what is included now suggests a reflection of a collection of historical and separate initiatives rather than a consistent approach. Some natural resources are paid for in different ways such as abstraction charges for water which are paid to the appropriate regulators. We suggest that there should be broader integrated approach and that there should be instead a natural resources or 'future generations' tax and incentive framework, which has the twin

objectives of behavioural change and paying to use resources. Furthermore the ambiguity of there being environmental elements in general taxes should be clarified and this should have a clear natural resources element as a subset. This should include a good understanding of how natural resources research and development should be included in tax allowances. There should be clear articulation of hypothecation. This change should be about better focussing management of resources and improving the environment and must not render the UK less competitive.

Cross Departmental Working

In order to effect these ideas, we commend the relevant Government departments, particularly BIS, DECC, and DEFRA to have an even closer relationship and of course the ONS and OBR providing objective data. We would also commend a better understanding by the Treasury of the impacts of restrictions on funding of the functions of Arm's Length Bodies via the Sponsoring Departments, without any further intrusion into the front line delivery of functions by those Bodies.

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