

Report by the (Ecofin) Council to the European Council in Barcelona on a strategy to integrate environment and sustainable development within economic policies

1. BACKGROUND

At its meeting in Cardiff in June 1998, the European Council invited all relevant formations of the Council to establish strategies to integrate environment and sustainable development within their policy areas. In Cologne (June 1999) the European Council specifically invited the Ecofin Council to develop a strategy for the integration of environmental issues and sustainable development within economic policies.

In responding to this request, the Council submitted as a first stage a report¹ to the Nice European Council in December 2000. This report builds on that first report. It is intended to respond to the invitation to the Council from the European Council in Gothenburg in June 2001 “to finalise and further develop sector strategies for integrating environment into all relevant Community policy areas with a view to implementing them as soon as possible”, and to “present the results of this work before the Spring European Council in 2002”. The report also takes account of the statement by the Stockholm European Council (Spring 2001) that the Broad Economic Policy Guidelines should “integrate the promotion of sustainable development”.

2. MAIN CONCLUSIONS OF THE COUNCIL’S REPORT TO THE NICE EUROPEAN COUNCIL

In its report to the Nice European Council, the Council observed that the Broad Economic Policy Guidelines, being at the centre of economic policy co-ordination, are well placed to develop a comprehensive, transparent and credible Community framework for improving the integration of environmental and sustainable development issues with economic policy. The Council recommended that the guidelines should encourage a consistent policy approach across sectors, based on an increased use of market-based instruments. It also called for the guidelines ultimately to include concrete objectives, timetables and mechanisms for monitoring progress.

¹ “Report by the (Ecofin) Council to the European Council in Nice on Environment and Sustainable development”; reference 13054/1/00 REV 1

3. PROGRESS IN IMPLEMENTING THE STRATEGY TO DATE

In stressing the importance of the Broad Economic Policy Guidelines as a means to foster the integration of environmental and sustainable development issues with economic policies, the Council sought to build on work which had already started in the 2000 guidelines. These were the first to include a separate section and recommendations on enhancing sustainable development. In this way, the Council took account of the conclusions of the Helsinki European Council which noted that the “Broad Economic Policy Guidelines provide the framework for the definition of overall policy objectives and orientations”.

The 2001 guidelines went further. They focussed on environmental sustainability to reflect the fact that other sections of the guidelines already deal with issues of economic and social sustainability. For the monitoring of the implementation of these guidelines, in the context of the Economic Policy Committee’s (EPC) 2002 country examinations on structural reforms, the EPC agreed that Member States should focus in their report on the use of market-based instruments in environmental policy. This was in line with the request made by the Council in its report on environment and sustainable development referred to above, and thus represents progress in implementing the proposals for a strategy set out in that report.

The outcome of these examinations is summarised in EPC’s Annual Report on Structural Reforms². The EPC Report notes increased awareness among Member States that market-based instruments are a means to make environmental policies more cost-effective, although in Community legislation, the traditional command-and-control measures still play a dominant part. Several Member States have implemented or plan higher fuel or energy taxes, though these efforts slowed down significantly in the wake of the oil price increase since 1999. In addition, some Member States are introducing tradable emission permits to combat greenhouse gas emissions. The use of subsidies or tax credits to promote investment in and the use of environmentally-friendly technologies is also becoming increasingly widespread.

However, the report shows that generally market-based instruments are still a supplement to regulatory instruments in environment policies. Furthermore, the report cautions that the implied lowering of costs through subsidies may increase overall use of energy and other natural resources by reducing the price of energy-intensive products, and recommends that further action should be taken to phase out subsidies to fossil fuel production and consumption. The report also notes a broad tendency to exempt energy intensive sectors from energy taxes. This may point to concerns about impacts on international competition based mainly on prices. Such promotion of special sectors increases the costs of fulfilling environmental targets. Action at Community level on, for example, minimum tax levels is identified as a means to remedy this inefficiency. Besides, Europe’s main trade partners should take steps towards protecting the global environment and meet the Kyoto targets. Generally, the report argues that existing taxes and excise duties, as well as certain public sector charges should be made more compatible with environmental concerns.

² “Annual Report on Structural Reforms”, (ECFIN/EPC/117/02-EN)

4. A COMPREHENSIVE STRATEGY TO INTEGRATE ENVIRONMENT AND SUSTAINABLE DEVELOPMENT WITH ECONOMIC POLICIES

A successful integration of environment and sustainable development with economic policies requires a strategic approach. Based on its report to the Nice European Council and on experience so far with the inclusion of environmental issues in the Broad Economic Policy Guidelines, the Council, in following-up to the request from the European Council, wants to point out:

- The overall aim of the strategy is to de-couple resource use and environmental pressure from economic growth in a way that reduces environmental pressure to sustainable levels without endangering sound economic growth.
- The polluter pays principle must become the heart of well-integrated economic and environmental policies. It reconciles best private costs of using natural resources with their social costs. Its appropriate application will give economic agents continuous incentives to use resources more efficiently, while ensuring a high level of environmental quality, and thereby contributes to the goal of the Lisbon strategy to “*become the most competitive and dynamic knowledge-based economy in the world capable of sustained economic growth with more and better jobs and greater social cohesion*”.
- Community legislation should leave Member States a high degree of flexibility in their choice of type and design of market-based instruments, as opposed to regulation, in environmental protection, as environmental and economic policies must increasingly rely on market mechanisms and market-based instruments. This will provide continuous incentives to all polluters to reduce pollution and reduce the total economic costs of reaching defined environmental targets. However, regulation and other non-market-based instruments have to continue playing a role where inefficient markets prevail, or where it is absolutely necessary that a specific environmental quality does not deteriorate below a certain level.
- The effectiveness of market-based instruments depends crucially on the competitive conditions and the price responsiveness of markets. Increasing competition by deregulating and interconnecting markets, lowering entry and exit barriers, and strengthening enforcement of competition laws will increase the efficiency of market-based instruments and should be pursued wherever appropriate.
- Cuts in distorting taxes, including labour taxes, could be introduced to compensate additional revenues from environmentally-related taxes and thus to prevent an increase in the overall tax pressure. The same should hold for expenditure savings, which result from the phasing out of environmentally harmful subsidies. By stimulating more efficient use of resources and reducing the relative price of labour, this could help to stimulate employment, in line with the Lisbon strategy.
- Wherever possible, policies should be announced in a timely fashion and be gradually implemented and with clear intermediate and final targets. The timely announcement will give planning security for economic agents, while the gradual implementation of policies will avoid to over-stretch the adjustment capabilities of the economy. Both will help to

avoid sudden changes in competitive conditions in which firms have to operate, while the guidance through clear targets will help to monitor implementation and achievements of this strategy.

- Wherever necessary, policies should be adopted and implemented in an internationally co-ordinated way, to avoid distortions in competition and the risk of environmentally counter-productive measures such as sectoral exemptions or derogations, which are usually not cost-effective. If exemptions are considered necessary, measures should be taken to limit their possible negative effects on the environment.
- Policy decisions at both EU and national levels should be based on sound analysis of their economic, environmental and social costs and benefits. In particular, the cost-benefit aspects of EU legislation should be strengthened. In this regard, the Council looks forward to the Commission's forthcoming Communication setting out how it intends to conduct such impact assessments.

While recognising the respective responsibilities of the EU and Member States in the area of taxation in accordance with Article 93 of the Treaty and the need for international co-ordination in order to avoid distortions of competition, the Broad Economic Policy Guidelines are the key instrument in the Council's strategy to integrate environment and sustainable development with economic policies. This should encourage a consistent approach across sectors, based on increased use of market-based instruments.

Having due regard to the principle of subsidiarity, the Council recalls that Member States should regard horizontal guidelines such as those on environmental sustainability as being addressed to them, and that accordingly, when reporting on their implementation of the guidelines, they should include information on the measures they have taken in respect of such horizontal guidelines. In this way, considerations of environmental sustainability should become part of the multilateral surveillance process and thereby integrated with economic policies.