

Are “environmental” tax incentives efficient?

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ABSTRACT

In Belgium, there are in fact two types of so-called environmental tax incentives in the field of energy. Some aim at energy efficiency, others at innovation. We examine to what extent these two types of incentives are justifiable on efficiency grounds. The theoretical concepts of market failure and externality are central to the discussion.

There are various market failures and externalities in the field of environment that are relevant to energy-efficiency policy. But we show that incentives are generally not the best instrument to address them. Market failures and externalities also apply to the field of green innovation. While energy taxation provides greater incentives for innovation, it does not remove these obstacles. This justifies the use of other instruments, which are subsequently examined.

All these issues come up clearly in the Belgian photovoltaics policy, which is presented as a case study. Although it can be judged positively in terms of innovation, two criticisms are levelled at that policy.

As a conclusion, the case for incentives in favour of innovation is strong, notwithstanding the fact that their design can be improved. As for energy-efficiency incentives, the case is much less convincing. Tax psychology might explain why they are in place.

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