

## C o m m e n t

# Encouraging more sustainable practice – the easy way.

Taking a lead from successful international schemes such as 'feebates' and Germany's best practice technology regulation, Australian governments could go further in implementing practical measures that create strong incentives for faster progress to more sustainable practice.

Economists are telling us that our high pollution levels and current unsustainable development trajectories arise partly from the fact that the real environmental and social costs of development are externalised from the market. Without these costs currently included in price signals, there is a legitimate role for government to act to ensure that these costs are actually accounted for and offset.

As Ken Henry, the Secretary Head of the Australian Treasury Department stated (in referring to what he had encountered as an economist), 'I learned about the importance of prices in guiding resource allocation. I came to the view that peoples' behaviour had a lot to do with their pursuit of self interest, and that a lot of what I might have found objectionable about the things humans did could have had something to do with the opportunities and incentives established by governments.'<sup>1</sup>

It is becoming clear that environmental degradation occurs because the current form of our economy makes it cheaper to degrade nature than to care for it.<sup>2</sup> These issues are now being widely discussed internationally.<sup>3</sup> They were also the subject of a 2001 Australian Treasury report<sup>4</sup> discussing how, for instance, the failure of individuals to properly consider social costs and benefits can mean that their

behaviour, while logical from their own point of view, will not, ultimately, be optimal from a social point of view.

Reflecting this, Ken Henry<sup>5</sup> said 'We go about our lives making many decisions based on cost – all of us base decisions on a formal or informal cost benefit analysis. When externalities are not present, the market price does not reflect the true costs of our decisions.'

As a case in point, international governments' policies, in keeping the price of water for farmers low, have led to excessive use of water, draining of water from underground basins which have built up over centuries, a consequential lowering the water table, and in some cases, leaching of the soil. In another example, in many countries, where much of the national timber lies on crown lands, the government, in making the land available, has paid less attention to concerns about long-term, economic efficiency than it has to the pleading of timber interest groups.<sup>6</sup>

Current market pricing, at present, just doesn't reflect the true cost to the environment and society of production, industry, and general consumption. But here, there is much government can do to fairly factor it in.

## Accounting in the outside costs

The basic solution usually promoted to 'internalise the real costs of externalities' is a levy, or an 'eco-tax'. European countries have used eco-taxes with great success. In Australia currently, however, any new tax is seen as unpopular by the major parties. Is there another way for government to at least provide specific incentives for more sustainable practice?

It seems so. Two ideas of note are 'feebates'<sup>6</sup> and Germany's Best Available Technology legislation.<sup>7</sup>

Feebates very simply combine both a fee on the most environmentally harmful brands of a certain products, thereby providing income to governments which facilitates a consumer-encouraging rebate on the most environmentally benign products.

Take the example of the concept applied to car use: when buying a new car you

would pay an extra fee if it were an inefficient user of fuel, or alternatively get a rebate if it were energy-efficient. The neutral point would be set so that fees and rebates balanced, and so it becomes neither an inflationary measure nor a disguised tax.

The fees and rebates may impact at the point of sale, or on annual registration fees, and usually offset each other ensuring fiscal neutrality. In principle, this can be a cost-neutral program to government, not involving any new taxes.

Encouragingly, Australian state governments in particular now have many rebate schemes to encourage consumers to purchase water and energy efficient products, but Australia does not have a single feebate scheme. Feebate variations already exist in Ontario (Canada), Germany, Denmark and Austria. In June 2004 France announced it would be implementing a feebate scheme on cars.

The key benefit of feebates is that they ensure industry knows there will be clear market signals to the consumer to purchase more efficient products, thereby stimulating innovation in the right direction for sustainability. But government would still need to work with industry to phase in feebates, giving industry time to respond.

To reduce administrative costs, feebates can first be targeted at those products that have the largest ongoing environmental impacts, such as cars, and household



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products such as refrigerators and washing machines. Such market signals can encourage car makers for instance, to move to producing hybrid cars rather than continuing with current models.

One drawback of feebates is that it is hard to accurately gage the external costs against which to set a fair fee and rebate amount, but this is true of any attempt to build in these complex factors into market signals.

The benefit of feebates over other attempts, however, is that they can be phased in before governments have fully detailed these parameters.

### A leading German solution

Industry is concerned that calls from sustainability experts to accommodate environmental and social costs may result in increased taxes on the key inputs to businesses, such as energy and water. Some industry groups, for instance, fear that an Australian carbon tax that

attempts to account for the negative environmental cost of CO<sub>2</sub> emissions, will lead to loss of competitiveness in key sectors, such as the mining industry.

The Germans, however, have developed an ingenious form of regulation that both helps drive better environmental outcomes whilst making German industry more competitive. The rest of Europe, including

Eastern Europe, have now followed Germany's lead.

The German Best Available Technology legislation does not involve mandating specific technologies as many in the other countries assume.

Rather, the German government upwardly adjusts standards that industry has to meet based on the performances of the best and most cost effective available technologies. In theory, whenever a new and improved technology is created globally, German industry is expected to meet the environmental standard achieved by that technology.

This regulation is sufficient to provide significant incentive for German firms to develop new technologies that make it cheaper for them to meet the competition from the best available technologies globally.

When this is coupled with regulation requiring continuous environmental improvement, auditing standards under EU regulation, feebates, and eco-taxes, it confers on Europe significant potential, long-term, competitive advantage in the field of environmental technologies.

Professor Michael Porter, from the Harvard Business School, wrote as far back as 1991, 'As other nations have pushed ahead, US trade has suffered. Germany has had perhaps the world's tightest regulations in

stationary air-pollution control, and German companies appear to hold a wide lead in patenting and exporting air-pollution and other environmental technologies. As much as 70 per cent of the air

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pollution-control equipment sold in the US today is produced by foreign companies.'

Britain is another case in point. As its environmental standards have lagged, Britain's ratio of exports to imports in environmental technology has fallen from 8:1 to 1:1 over the past decade. In contrast, the US leads in those areas in which its regulations have been the strictest, such as pesticides and the remediation of environmental damage.

Such leads should be treasured and extended. Environmental protection is a universal need, an area of growing expenditure in all the major national economies, and a major export industry. The strongest proof that environmental protection does not hamper competitiveness is the economic performance of nations with the strictest laws.'

Feebates and Germany's Best Available Technology legislation are just some examples of the range of innovative and flexible approaches through which government could take a stronger lead ahead of industry and the community to achieve sustainable development.<sup>8</sup> There have been encouraging signs recently that environmental and wider societal quotients are at last being acknowledged in rebates for more relatively environmentally friendly products; the time is now right for leadership on trials of more of these low-risk but simple and effective solutions across Australia.

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### More information:

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1 Ken Henry, Head of Treasury Australia, Speech to the 30th Anniversary of the ANU Masters Program.

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2 Daily, G.C. and Ellison, K. (2002). *The New Economy of Nature: The Quest to Make Conservation Profitable*. Island Press, Washington.

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4 Economic Roundup, Treasury Department (2001). Public Good and the Impact of Environmental Measures Imposed On Landholders, p. 93

5 Ken Henry, Head of Treasury Australia, Speech to the 30th Anniversary of the ANU Masters Program.

6 von Weizsäcker, E., Lovins, A. and Lovins, H. (1997). *Factor Four: Doubling Wealth, Halving Resource Use*. Earthscan, London.

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8 These ideas, and many more practical ones like them, are further discussed in a forthcoming book: *Natural Advantage of Nations, Business Opportunities, Innovation and Governance* by the Natural Edge Project ([www.naturaledgeproject.net](http://www.naturaledgeproject.net)), a multi-stakeholder project including CSIRO, Engineers Australia, Rocky Mountain Institute, and Natural Capitalism Inc. to name some partners. It involves a range of projects dedicated to capacity building and education for sustainable development. The book shows, for instance, that these sorts of wise leadership initiatives from governments can help nations decouple environmental damage from economic growth, whilst increasing the global competitiveness of their businesses.