

Case Study: Trade Tax Reductions for Cleaner Production at Municipal Level

What are Trade Tax Reductions for Cleaner Production?

A proposal for trade tax reductions at the municipal level in Paraguay was put forth within the framework of a Technical Cooperation initiative between the MERCOSUR trade organisation and Germany. The MERCOSUR or “Common Market of the South” was founded in 1991 by Argentina, Brazil, Paraguay and Uruguay. The principal idea of this cooperation project is to promote cleaner production in cities and municipalities and thus create win-win situations whereby companies can reduce tax burdens while municipalities face reduced environmental pollution from industrial activities.

How are the tax reductions designed to work?

In Paraguay, a major part of municipal revenue consists of a trade tax, paid by large industries based on their annual turnover. In close cooperation with three medium-sized cities - Caaguazú, Villarica and Coronel Oviedo - an economic instrument was designed that intended a step-wise tax reduction (to a maximum reduction of 20% of tax payable) for those industries that implement cleaner production programmes and can actually demonstrate measurable and independently verified results such as emission reduction, pollution minimisation or increased natural resource use efficiency.

The implementation of the instrument required a modification of the municipal tributary ordinances so that the reduced municipal tax income may be compensated within the framework of evaluation and verification procedures and related fees. On the whole, the design of the system provides advantages to enterprises that make steady advances under a cleaner production programme. The introduction of the tax reduction is required to be accompanied by awareness building, information and training measures for public authorities, industries and independent consultants.

Evaluating the tax reduction model in Paraguay

Due to the early stage of project implementation an evaluation of the operation of the programme is neither existing nor possible. However, it is clear that political lobbying and awareness building are required in order to convince local politicians of the benefits of the model. Nevertheless the existing interest among different municipalities demonstrates that there is a demand for the model and that the chances of replication are good. Apart from environmental benefits and efficiency gains, the possibility of compensation for lower municipal tax revenues and the creation of local capacities for environmental management are crucial elements.

Good training and information work is necessary for successful application. Last but not least, a comprehensive monitoring system is important to guarantee the proper development of the instrument in its introduction phase. In the case of Paraguay a supporting factor has been the compatibility with the ongoing general decentralisation of environmental management that is being supported by, among others, the Inter-American Development Bank.

Further information

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See also the following publications, jointly edited by the MERCOSUR Working Group on Environment (SGT

No. 6 – Subgrupo de Trabajo Medio Ambiente) and the GTZ:

“Gestión Ambiental y Producción Más Limpia en el MERCOSUR – Logros Alcanzados en los dos Primeros Años del Proyecto Competitividad y Medio Ambiente” (2004, Spanish / Portuguese)

“Elementos de Política y Herramientas de Gestión Ambiental y Producción Más Limpia en el MERCOSUR” (2004, Spanish / Portuguese)

The joint project “Competitiveness and Environment” is carried out by the MERCOSUR Working Group for Environment and GTZ in close cooperation with the Working Group for Industry and private sector organisations. The objective of the project is to establish and implement a common strategy for cleaner and more efficient production patterns. Working areas include policy development, public-private cooperation as well as practical efforts and the exchange of experiences in cleaner production, resource efficiency and environmental management. Economic instruments and incentives are considered a key element, particularly to integrate environmental and economic policies and to address small and medium-sized enterprises (SMEs), which are a key target group.

The approach to market-based instruments under the project could be characterised as ‘down-to earth’ and oriented towards pragmatic mechanisms that can be implemented with relatively minor changes to existing legal frameworks and/or promotion schemes to make them work (more effectively) for sustainable production. Baseline studies on competitiveness and environment within MERCOSUR and at the member state level in 2002 / 2003 have shown significant differences between the countries and suggest a country-specific approach. Following experience sharing seminars between MERCOSUR countries, including expertise drawn from Chile and CEPAL, studies were launched at the national level in order to identify instruments that could be implemented within relatively short time.

With their differing situations the recommended instruments vary considerably from one country to another. The proposal for Argentina aimed at integrating cleaner production explicitly into existing SME promotion schemes. It was suggested that Uruguay should develop primarily market-based instruments in the areas of industrial waste water and solid waste, directly related with its general law on environmental protection. However, the approach in Paraguay described above aims at the municipal level and is coherent with general decentralisation efforts in environmental management. In addition to the mentioned instruments, soft incentives like cleaner production awards are promoted and at the MERCOSUR level the use of a future structural fund for the promotion of sustainable production was evaluated.