

"Emission Quotas" and "Paid Use" Require a Good Institutional Interface

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Abstract: As a typical market measure to protect the environment, the trading of emission rights originated from the control of sulfur dioxide under the Clean Air Act of the United States. In this article, the author suggests that the paid use of "pollutant discharge right" in China should be effectively connected with environmental taxes and fees to avoid the phenomenon of imposing double economic burden on the same pollutant discharge behavior of enterprises. Also, the paid use of "emission quotas" needs to take into account the reduction of emission quotas.

1. Introduction

The trading of "emission quotas" began with the control of sulfur dioxide under the US Clean Air Act. The trading of "emission quotas", as a typical market measure aimed at protecting the environment, began with the control of sulfur dioxide under the US Clean Air Act. Since 2007, 11 provinces (cities), including Hebei, Tianjin and Inner Mongolia, have been officially organized by the relevant departments of the State Council to carry out pilot projects on the paid use and trading of "emission quotas". On this basis, in August 2014, the General Office of the State Council issued the "Guiding Opinions on Further Promoting the Pilot Project on the Paid Use and Trading of Emission Quotas" (Guo Ban Fa [2014] No. 38) (hereinafter referred to as the "Guiding Opinions"), which further launched the pilot project on the paid use and trading of "emission quotas" nationwide. In the initial allocation of emission quotas on a pilot basis in China, the government is required to allocate the total amount of emissions among enterprises for a fee, and the issue of the interface of the system for the paid use of emission quotas needs to be resolved.

2. The Paid Use of Emission Quotas Should Be Effectively Linked to Our Environmental Tax System.

The paid use of emission quotas implemented on a pilot basis in China is actually a way for enterprises to buy emission quotas from the government and then discharge within the limits of their emission quotas. According to China's relevant regulatory documents, the paid use of "emission quotas" reflects the idea that the environment has a price, and that the environment is no longer a free good, in line with the requirements of China's ecological civilization construction to strengthen environmental protection. However, in practice, there has always been a corresponding tax and fee system in the field of environmental protection in China, and the environment has never been a public good to be used for free.

The Environmental Tax Act transformed China's sewage charge system into an environmental tax system. However, whether it is an emission fee or an environmental tax, from an economic point of view, both are a means of internalizing the negative environmental externalities of enterprises, and in a sense both embody the idea of paid use of the environment. According to the provisions of China's Environmental Tax Law and other relevant laws, an emitter who directly discharges taxable pollutants into the environment shall pay environmental tax; an emitter who indirectly discharges taxable pollutants into the environment shall pay pollutant treatment fees to a third party pollutant treatment agency, although he/she does not pay environmental tax. Thus, environmental taxation is essentially a measure for enterprises to internalize the negative environmental externalities of their production activities, reflecting that they are paid for the use of environmental capacity. At the same

time, the paid use of “emission quotas” for key pollutants implemented on a pilot basis in China is also a paid use of environmental capacity, which in essence is also a way of internalizing the negative environmental externalities of enterprises' production activities. Therefore, the functions of environmental taxes and fees are consistent with and duplicate those of the paid use of emission quotas. Moreover, both the Guidance and local legislation clearly stipulate that “units that have acquired emission quotas for a fee are not exempted from the obligation to pay sewage charges and other related taxes and fees in accordance with the law”. In other words, if an enterprise directly discharges key pollutants to the environment that are subject to total control in a certain place, it will have to pay both environmental taxes and purchase emission quotas; if an enterprise indirectly discharges key pollutants to the environment that are subject to total control in a certain place, it will have to pay both pollution treatment fees and purchase emission quotas. In either case, the enterprise is charged twice for the same amount of emissions, thus increasing the economic burden on the enterprise and making it unfair. If an enterprise emits non-priority pollutants, it does not need to purchase emission quotas as it does not apply total volume control, and only needs to pay environmental protection tax in accordance with the relevant provisions of the Environmental Protection Tax Law. However, both enterprises emitting priority pollutants and enterprises emitting non-priority pollutants have to use environmental capacity for the pollutants they emit, and all of them have a certain impact on the quality of the environment. However, enterprises emitting priority pollutants are required to pay twice for the use of their environmental capacity, while enterprises emitting non-priority pollutants are only required to pay once for the use of their environmental capacity. In terms of time sequence, the environmental tax and fee system comes first and the paid use of “emission quotas” comes second, but the paid use of “emission quotas” in China does not take the environmental tax and fee system into account, thus unreasonably increasing the burden on enterprises.

In view of this, I suggest that the paid use of “emission quotas” in China should be effectively connected with environmental taxes and fees, so as to avoid the phenomenon of imposing a double economic burden on the same emission behaviour of enterprises. Specifically, there are two main ways of linking the paid use of emission quotas and environmental taxes.^① Replacing the “right to use” fee with an environmental tax. This measure is mainly based on the scope of taxable pollutants as stipulated in China's environmental protection tax law, and determines whether the acquisition of a certain pollutant emission quota should be subject to a fee. If the pollutant for which the quota is issued is a taxable pollutant under the Environmental Protection Tax Law, the enterprise will only be required to pay the environmental tax in accordance with the provisions of the Environmental Protection Tax Law, and will not be required to pay a separate fee for the emission quota it has been issued. In other words, the administrative department in charge of environmental protection will no longer charge a separate fee for the issuance of emission quotas for taxable pollutants. If the pollutant for which quotas are imposed is not a taxable pollutant under the Environmental Protection Tax Law, the enterprise will be required to pay a fee for the emission quota for that pollutant. However, in reality, it may be difficult to find pollutants that are not taxable pollutants under the Environmental Protection Tax Law for which quotas are imposed on enterprises. This is because the pollutants that are subject to total control and therefore to quotas are already priority pollutants, and such priority pollutants are generally unlikely to be taxable under the Environmental Protection Tax Law. Therefore, this option is in effect an environmental protection tax instead of an emission quota fee. The enterprise would only need to pay environmental tax to the tax authorities on the pollutants it emits in accordance with the provisions of the Environmental Protection Tax Law. If the environmental tax paid by the company is not taken into account, the company gets the emission allowances for free just in terms of whether it pays the emission allowance user fee or not. This is also the “grandfather principle” in the initial allocation of emission allowances in the US, i.e. companies receive their emission allowances free of charge based on their historical emissions.^② The environmental tax paid by the enterprise is deducted from the primary market royalty for the “emission quotas”, i.e. the actual royalty paid by the enterprise for the emission allowances is the difference between the initial fee paid by the environmental protection authority for the grant of the

emission allowances and the environmental tax payable on the emissions of the allowances. In reality, if the environmental quality of a certain area is poor, the pressure on environmental protection is high and the environmental protection administrative department feels that the environmental protection tax paid by the enterprise is not sufficient to reflect the cost of using the environmental capacity of a certain pollutant, then the initial allocation of emission quotas can be made by way of listing or auction. In this case, the enterprise should deduct the environmental tax payable on the emission quotas it receives from the cost of the initial allocation of emission quotas. In reality, all provinces in China that have implemented pilot trading of emission allowances basically allocate the initial allocation of emission allowances by means of a “fixed-rate offer”, and apply differential prices and “emission allowances” to different regions. However, the environmental tax payable by enterprises is not deducted from the “emission quotas” user fee, thus making the “emission quotas” user fee and the “emission quotas” user fee incompatible. There is no linkage between the “emission quota” user fee and the environmental tax. In reality, we should allow each region to determine which option to choose based on its own environmental quality and level of economic and social development. However, the first option would be more effective if the government were to make the necessary and timely reductions in the emission quotas of enterprises in order to protect the environment in a timely and effective manner.

3. The Paid Use of Emission Quotas Takes into Account the Reduction of Emission Allowances.

In our pilot practice, the emission quotas acquired by enterprises are considered as a property right of the enterprises, and this property right is acquired for a fee. According to the rule of law, the emission quotas of enterprises should be effectively protected by law as a private right of enterprises, and cannot be reduced by the government and its departments arbitrarily, except for justified reasons and through due process. However, both in theory and in practice, the use of an enterprise's emission quota should be entirely for the purpose of ensuring that environmental quality standards are met. Therefore, in the event of exceptional weather conditions that lead to a sharp reduction in environmental capacity, the government should be able to reduce an enterprise's emission quota in time to meet environmental quality objectives. In cases where emission quotas are a legal property of the enterprise, the reduction of the enterprise's emission quotas is effectively tantamount to expropriating the private property of the enterprise. This is seen as a complex matter requiring prudence in a modern society governed by the rule of law. Therefore, paid use to a certain extent reinforces the rights-based nature of emission quotas and makes it more difficult for the government to impose reductions on them at any time.

From the current practice of paid acquisition and trading of “emission rights” on a pilot basis in various parts of China, the more common practice around the country is to allow the government to “buy back” the “emission rights” of enterprises under certain conditions. The practice is that the government is allowed to “buy back” an enterprise's emission rights under certain conditions. If taken literally, government buy-back reflects the government's management and control of enterprises' emission quotas, and can be applied to situations where the total amount of enterprises' emission quotas exceeds their environmental capacity due to extreme weather, reflecting the original intention and purpose of the system for environmental protection. However, judging from the relevant provisions of the management methods for the paid acquisition and trading of emission rights implemented by various provinces and municipalities in China, the government's buy-back of enterprises' emission rights is a way for the government to reserve emission rights. The core meaning of the buy-back of the government's “emission rights” as a way for the government to reserve “emission rights” is not to reduce the government's emission quotas for enterprises in extreme weather conditions to ensure that environmental quality standards are met, but to “activate and regulate the market, or to guarantee the construction of strategic emerging industries, major scientific and technological demonstrations, major livelihood projects, etc. “to be able to start smoothly.

4. Conclusion

Therefore, to formulate China's emission quota trading system in the future, we must make up for the deficiencies in the current pilot practice, stipulate the reduction of emission quotas, and clearly stipulate the conditions for reducing emission quotas. The reduction of enterprise emission quota must be a compulsory measure taken by the government for the purpose of environmental protection under specific circumstances. If the enterprise's emission quota is obtained free of charge, the compulsory reduction of its emission quota does not need to compensate the enterprise for its interests; If the enterprise's emission quota is paid, the compulsory reduction of its emission quota must provide certain interest compensation to the enterprise, and the compensation standard should not be lower than the acquisition cost of the reduced emission quota at least.

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