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REPORT

ON

THE TRANSITION TO A GREEN ECONOMY:

A REVIEW OF DISTRIBUTIONAL EFFECTS IN EUROPE

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[1] All positions and views expressed in the paper are of the author.

EXECUTIVE SUMMARY

The green transition is a formidable challenge for all European nations, especially now with the war of aggression against Ukraine giving rise to economic uncertainty and higher energy prices across Europe. The effects of the transition will vary from country to country and from region to region, depending on a host of economic and social variables.

This report looks at the likely effects of the transition in terms of social exclusion and income inequalities (Chapter 1) and reviews relevant policies in a context of a just transition for low-income households and vulnerable groups (Chapter 2).

The success of the green transition calls, above all, for collaboration across Europe, with the European Commission and the Council of Europe playing a leading role not only in facilitating the transition but also by providing guidance on income support measures to promote social cohesion (Chapter 3).

Social dialogue and the democratisation of institutions that allow the involvement of civil society and non-governmental organisations in decision-making are essential in developing social cohesion policies. Again, the Council of Europe could play a leading role in advising European countries on the legal and institutional frameworks required for effective social dialogue (Chapter 4).

In this connection, it is also necessary to consider the impacts of the green transition on employment and how governments, in consultation with civil society, could develop or re-energise active labour market policies in Europe to support the transition. How the labour market responds to the transition is crucial since millions of workers (especially those working in carbon-intensive industries) are likely to be impacted by the transition (Chapter 5).

It is also important to be wary of the possible additional costs arising from the transition, particularly on commodity prices that could be impacted, as in the case of transport. It is necessary therefore to consider measures such as reducing the tax burden on low-income households and vulnerable groups. Tax reform, targeted income-support measures, and increased market competition could contribute to price stability (Chapter 6).

During the transition, it is pertinent to recognise that the effects of transition will vary both between and within countries. As a result, the measures required to support social cohesion will vary from country to country and from region to region. Nevertheless, a common framework under the direction of the Council of Europe to support institutions and provide funding, is deemed necessary (Chapter 7).

In line with the above, the report provides five timely recommendations aimed primarily at addressing the challenges to social cohesion arising from the green transition.

INTRODUCTION

The transition towards a green economy in Europe is one of the most ambitious European projects ever. Specifically, the European Green Deal marks an important step in the EU's efforts to tackle climate change. Non-European Union (EU) countries in Europe are also bound by the Paris Agreement climate change commitments but, unlike EU Member States, they have fewer financial resources at their disposal to implement the changes required in the energy and transport sectors. This could result in a number of non-EU European countries lagging behind the targets set by the EU for its Member States.

The Green Deal increased the EU's 2030 greenhouse gas (GHG) emissions reduction target from 40% to at least 55% below 1990 levels, setting a target of climate neutrality by the middle of the century. Last year, the European Commission presented its "Fit for 55" package which contains a series of policy proposals for meeting the 2030 target.

The proposals include a reduction in the allowances in the existing Emissions Trading System (ETS) (i.e., for industry and power sector emissions), the introduction of a new trading system for building and road transport emissions, and more ambitious national targets for sectors covered by the Effort Sharing Regulation. They also involve the introduction of a Carbon Border Adjustment Mechanism (CBAM).

What is clear is that countries and households will not be impacted in the same way by efforts to accelerate decarbonisation up to and beyond 2030.

1. The effects of the transition: social exclusion and income inequalities

The potential distributional effects across Europe will vary depending on a number of economic and social considerations. However, these considerations can be summarised as follows: (i) growing income disparities; (ii) the relocation of industrial sectors and related jobs; and (iii) growing regional disparities. At the EU level, the potential distributional effects could be: (i) a further deepening in the gap between more advanced economies and those that are still heavily reliant on carbon-intensive industries, as well as between the urban areas and the more remote regions; and (ii) increased migratory flows and greater tensions caused by immigration, as well as the further depopulation of remote regions.

At the pan-European level, the potential distributional effects are likely to be a mix of the above, with a potential additional effect arising from the possible displacement of polluting industries to the "less restrictive regimes" mainly in non-EU European countries. Before Russia's war of aggression against Ukraine, Russia's Gazprom was planning to introduce an emissions-free form of hydrogen into its business over the next few decades. That would have helped the EU to reduce emissions by 62% by 2050, a significant portion of the EU's commitment to slash pollution by 80% below 1990 levels by 2050.[2]

This has, of course, all changed with Russia's war of aggression against Ukraine. There are three aspects to consider: (i) Russia's reputation as a reliable supplier of natural gas; (ii) the reconstruction of Ukraine in a post-war scenario; and (iii) the economic and financial ramifications

[2] https://www.bloomberg.com/news/articles/2018-11-08/russia-looks-to-hydrogen-as-way-to-make-gas-greener-for-europe

of the war itself which may lead to the EU and other non-EU European countries revising plans for transitioning to a greener and more sustainable economy. According to the World Bank[3], the reconstruction of Ukraine after the devastation Russia has inflicted upon it will require a huge international effort to the tune of $349 billion to help rebuild and resuscitate its economy. This could present an opportunity to make a leap forward in terms of green energy sources. Coal has, until now, been the second most important source of electricity production in Ukraine (after nuclear energy). If Ukraine were to abandon coal as a source of electricity, it would have to be replaced by cleaner and renewable forms of energy. We do not, however, yet know the outcome of the war, nor do we know whether or when regions like Donbas will be reintegrated into the internationally recognised borders of Ukraine. If parts of Ukraine were to remain under Russian occupation, they would not be part of the reconstruction effort and Russia could allow these annexed territories to use coal as an energy source. The implication of this is that large parts of Europe might not participate in the green transition.

As recently stated by the Eurofound,[4] Russia's war of aggression against Ukraine and the resulting sanctions have caused energy prices to soar. Governments seeking to alleviate the negative impacts on households of the price increases have introduced energy subsidies and VAT reductions for electricity, gas, and fuel. While such policies may be needed to protect those most in need, Eurofound argues that subsidising energy use is a short-term solution – it is a temporary, partial compensation that may not always reach those who are hardest hit. Added to this, subsidising fossil fuel energy use runs counter to the EU's aims of limiting carbon emissions and maintaining its energy dependency on third countries, such as Russia.

Eurofound also argues that the problem of high energy prices could be addressed in tandem with the EU's climate policy and its geopolitical interests. This, however, would require governments to shift from energy subsidies to investing in reducing households' and businesses' energy needs and dependence on energy from external sources. The challenge here is that achieving this requires a length of time and a considerable outlay of financial resources. This could disproportionately increase the social cost or burden of the transition on poorer households across Europe, including in EU Member States. It should be noted that EU climate policy is intended to reflect the principle of fair burden-sharing across and within countries. In this regard, it should be recalled that the EU has agreed to set aside funds for the Social Climate Fund,[5] as well as the Just Transition Fund,[6] to mitigate any negative effects on vulnerable groups and poorer households, and on economic sectors that are still heavily dependent on fossil fuels.

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[3] https://www.grid.news/story/global/2022/09/15/the-ukraine-war-in-data-349-billion-the-low-estimate-for-rebuilding-ukraine

[4] https://www.eurofound.europa.eu/publications/blog/shifting-the-focus-from-energy-subsidies-to-reducing-energy-dependence

[5] The Social Climate Fund is intended to finance temporary direct income support for vulnerable households and to support measures and investments that reduce emissions in road transport and the building sectors and, as a result, reduce costs for vulnerable households, micro-enterprises and transport users.

[6] The Just Transition Fund supports the economic diversification and reconversion of the territories concerned. This means:
– investments in small and medium-sized enterprises
– creation of new firms
– research and innovation
– environmental rehabilitation
– clean energy
– up- and reskilling of workers
– job-search assistance

Meeting the challenges of climate change and environmental sustainability could be even more difficult in non-EU European countries. The speed and scale required to successfully implement the green transition will entail challenges for all Council of Europe member States. Take the example of Serbia. The challenges from the green transition faced by Serbia include the impact on regions affected by the decline of fossil fuel sectors which cannot easily adapt to a greener economy. As the European Bank for Reconstruction and Development's publication "Just Transition Diagnostics: Serbia" points out, this is of particular concern where workers have few alternative employment opportunities. There is also concern that the transition could lead to higher commodity price rises, especially for poorer households.[7]

In general, and this applies to all Council of Europe member States, countries and regions will face different impacts depending on their level of socio-economic development. The costs of the transition may fall unevenly and may not correlate with the benefits. For instance, regions with a high dependency on carbon-intensive fuels are particularly exposed to the impact of the transition and to potential job losses.

Concerns over those negative regional impacts necessitate a focus on a transition that factors in the impacts on households and businesses that rely heavily on carbon fuels. The shift towards a climate-resilient and low-carbon economy is particularly challenging for low-income households and communities in regions of a country where the level of development lags behind the urban areas. It is therefore vital that the transition is underpinned by a battery of measures providing financial support to address the concerns expressed above.

Clearly, the shift towards a greener and more sustainable economy is an important goal, but achieving it is a formidable challenge that could be derailed by the economic and financial shocks caused by the war of aggression against Ukraine. This implies that the financial resources to support a just transition towards a green economy may not be forthcoming.

It should be noted, however, that the European Bank for Reconstruction and Development (EBRD) is working with a number of countries to plan how the Bank can provide support, from a policy and capacity-building perspective, thereby indirectly providing support for a just transition in non-EU cities and regions. Capacity building for investments to support the green transition is critical. In the initial stages, the EBRD carries out a just transition diagnostic study to identify the main challenges of the transition and the likely social and economic effects.

In this connection, the EBRD is working with other agencies (such as the EU and the World Bank) on the topic of just transition and is conducting studies for a number of countries in the Western Balkans. This is part of the coordinated action led by the EBRD aimed at supporting the transition in those regions still dependent on coal for their energy requirements. This coordinated action covers the West Balkan region and not just Serbia.

The EBRD initiative for Serbia could therefore be replicated in other non-EU countries. The diagnostic study for Serbia analyses how the transition towards a green economy in the country can be accelerated while also managing the social and economic effects of the transition, focusing on the regions, industries, communities and vulnerable groups facing the greatest challenges. The analysis provides the Serbian Government with four key outcomes:

– transformation of existing carbon-intensive installations

[7] BERD, « Just Transition Diagnostics: Serbia », https://www.ebrd.com/work-with-us/projects/tcpsd/14896.html

(1) Analysis of the economic, social and environmental situation assessed at local and national level;

(2) Analysis of the financial, economic, social, gender, health and environmental impacts of a green transition;

(3) A set of budgeted actions to support a just transition in Serbia; and

(4) A Just Transition Action Plan that will include recommendations for strengthened institutional and governance structures, the implementation of the necessary policy reforms to support a just transition, and proposals for potential targeted investments.

All of the above is highly relevant and commendable. However, as pointed out earlier, this plan of action risks being derailed by the effects of the war of aggression against Ukraine and its economic and financial consequences, especially the increasing budgetary pressures caused by financial support aimed at mitigating the effects of rising energy and food prices.

2. Inclusive policies and a just transition

Climate change threatens us all but, like the pandemic, it has a more damaging effect on the most vulnerable and marginalised people. The deterioration of the environment has an undeniable impact on the enjoyment of many social rights [provided under the European Social Charter], such as – for example – the right to health and the right to safe and healthy working conditions, or the right to adequate housing, the right to work, and the right to protection against poverty and social exclusion.[8]

It is crucial, therefore, that the transition leaves no one behind. Leaving no one behind entails re-empowering as many people as possible to play a positive role as active citizens, maximising the accessibility of investments, new lifestyles, consumption patterns, and sustainable technology for all people, groups, and regions during the transition process. This starts with setting up the appropriate governance structures and tools to drive the transformation, developing a wider understanding of the "just transition", with the full implementation of the European Social Charter[9] and the European Pillar of Social Rights to support it, while driving forward reforms of redistributive systems, as well as of work-life balance and gender equality.[10]

It is with this in mind that the European Commission stresses the need for appropriate accompanying policies to reduce - and even prevent - energy poverty, which stems from a combination of factors including low income, a high share of disposable income spent on energy and the poor energy efficiency of housing.

As previously mentioned, non-EU European countries face similar challenges in achieving a just transition and are relying on the EBRD to understand the likely impacts of the transition towards a green economy. The EBRD's diagnostic study could be highly relevant in the case of non-EU

[8] Giuseppe Palmisano, *The ESC system and protection of the environment: Potential and future prospects*

[9] The European Social Charter (revised) is a Council of Europe treaty which guarantees fundamental social and economic rights of all individuals in their daily lives.

[10] The European Pillar of Social Rights (EPSR) is a set of documents containing 20 key principles and rights intended to build a fairer Europe in the fields of labour markets and welfare systems.

countries and is a somewhat similar approach to the impact assessments conducted by the European Commission for the EU in connection with the “Fit For 55” package.

In addition, accompanying policies can promote access to affordable and low-emission transport and mobility options, tackle social exclusion and socio-economic, regional and health inequalities, improve health and well-being, and promote equality in general and also for disadvantaged persons. What is at stake here is not only the development of policies but also their effective implementation. This requires a commitment on the part of members of the Council of Europe to provide adequate funding to tackle social exclusion and reduce inequalities. This also requires a significant effort on the part of government welfare agencies to identify those within communities who are likely to be impacted negatively by the transition and to fully understand the resulting distributional effects.

To realise the green transition’s full employment and social potential, it is essential to use all available tools and to put in place the appropriate accompanying labour market and social policies in European cities and regions. Such policies need to be applied consistently and systematically across the entire continent. Otherwise, the climate neutrality targets cannot realistically be achieved. If non-EU European countries do not make the transition as effectively as EU Member States (though there is no guarantee that the transition in the EU will be successfully implemented), EU countries may face a movement of people in their direction, particularly from the Western Balkans area and its poorer cities and regions.

Without well-crafted accompanying employment and social policies, the socio-economic risks of the transition would be significant, leading to widening income inequalities, especially in European countries where trade union membership and collective bargaining coverage are relatively low.[11] The role of trade unions in mitigating rising income inequality, as observed in advanced economies in recent decades, has in fact been somewhat overlooked in empirical studies, despite its theoretical ambiguity. In the paper cited in the footnote and published in the International Labour Review, the authors examine the relationship between trade unions and income inequality in European countries (including non-EU Member States) and conclude that trade union action has been relevant and effective over time.

The baseline empirical model, estimated for a panel of 26 European countries over the period 2005 to 2018, specifies income inequality as a function of the trade union density rate, its squared value, and a set of control variables. Labour market institutions other than unions, such as employment agencies and relevant regulatory authorities, are then incorporated within the model to assess the distributional effects of union density and how union density affects income inequality. The authors found a statistically significant and persistent inverted U-shaped relationship between unionization rates and income inequality, shedding light on the conflicting results reported in previous studies, referred to in the paper (see footnote 3). This conclusion highlights the potential role of trade unions, as well as employment policies, in addressing deepening socio-economic divides at a time when the transition towards climate neutrality is gaining momentum.

In addition to employment policies, it is also highly relevant to refer to the importance of welfare and redistribution policies which help avert social exclusion. In the context of the green transition, welfare policies need to be targeted and focused on the social cost of the transition. Using the

[11] See Montebello, R; Spiteri J; and von Brockdorff P: *Trade Unions and Income Inequality: Evidence from a Panel of European countries*.

term “targeting”, this report relates to low-income households and various groups in vulnerable situations, such as older persons and persons with disabilities. To support welfare policies, as described above, redistribution measures that allow for financial resources to be directed towards assisting low-income households and persons in vulnerable situations need to be in place. These could take the form of environmental taxation based on the “polluter pays principle” with income earners above a given threshold paying higher tariffs for consuming carbon-intensive energy. This approach, based on the progressive tax system, could be extended to environmental taxation to support the transition towards a green economy.

It is crucial that the competent authorities put in place appropriate policies, and do so with the above in mind, but without undermining the incentives for the changes in investment and consumption required by the transition. Importantly, such mechanisms should be accompanied by measures to ensure inclusive governance, prioritising a transversal approach to human rights and the active involvement of those most affected by the green transition. This will require undertaking impact assessments on the likely impact of the transition on economies and communities across Europe. Such impact assessments have been carried out in the EU by the European Commission. These assessments are important, although they lack the depth required on a country by country and region by region basis. A more in-depth analysis would provide a more detailed and more relevant assessment of impacts. Moreover, they would deliver information on households affected by the transition, allowing governments to take measures to mitigate and offer support to poorer households who would bear the brunt of the transition.

It should be stressed that the political and social acceptance of climate policies within European countries will lose its legitimacy if the burden falls disproportionately on poorer households.[12] It also needs to be acknowledged that climate change, as well as migration (so called climate refugees) will raise a host of additional social rights issues and adaptation measures, will create winners and losers, exacerbating social inequalities. For this reason, European countries need, above all, to recognise this and commit themselves to leaving no one behind, as stated earlier. There needs to be a just transition that addresses both the employment and distributional effects of the shift to climate neutrality or whatever state may be closest to that. This should be seen as an integral part of the climate policy framework (*e.g.* the “Fit for 55” package in the EU) and not only as a series of supplementary corrective measures. These issues span many dimensions, such as the distributional effects of decarbonisation policies, job losses, and employment transitions, the protection of basic social rights and the inclusion of all citizens and organised civil society in decision-making.

The latter is of course a challenge in any country but particularly in those EU Member States and non-EU European countries where the voice of civil society in a number of cases is weak or virtually non-existent. Moreover, and this applies particularly in non-EU European countries, the absence of an effective, fully functional institutional framework makes it more difficult to draw up effective policies and meet the challenge of the transition with measures based on the feedback from civil society, especially non-governmental organisations representing low-income households and groups in vulnerable situations. The EBRD diagnostic study conducted in Serbia mentioned earlier could serve as a model to be adopted in non-EU European countries.

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[12] See Büchs, M., N. Bardsley and S. Duwe (2011), *Who bears the brunt? Distributional effects of climate change mitigation policies*, Critical Social Policy Vol 31, 2011, pp. 285–307.

As far as the EU is concerned, the importance of the Just Transition Fund cannot be understated. This financial instrument aims to address the socio-economic impact of the transition in EU economies heavily reliant on fossil fuels or greenhouse gas-intensive industrial activities, but the objective is, above all, to cushion the effects of the transition for workers and households most affected. The EU also set up a Just Transition Platform to support all the relevant stakeholders to make use of the resources of the Just Transition Mechanism.

In addition to the Just Transition Fund (Pillar 1), the Just Transition Mechanism contains a dedicated scheme under Invest EU (Pillar 2) and a public sector loan facility (Pillar 3). Whether all this will be sufficient to support the transition is debatable, especially in light of the war of aggression against Ukraine and its effects on prices. That said, the EU proposal could serve as a model for all European countries, assuming that a coordinated approach can be agreed and implemented across all European countries, EU Member States or otherwise. It remains to be seen whether an agreement on this will be reached. Nevertheless, as mentioned earlier, the EBRD can provide funds for non-EU European countries to identify and help address the challenges of the transition.

3. Collaboration across Europe

The transition process under way across Europe (albeit at different levels of commitment and with varying accompanying policies) risks being derailed by two extraordinary events: the COVID-19 crisis and the fundamental change in Europe's geopolitical situation due to Russia's war of aggression against Ukraine. Both have further increased the burdens on communities, particularly with regard to energy and food prices. The war of aggression against Ukraine may prove to be too great a challenge for the rest of Europe, and the risk that the transition will lose impetus and focus is a real one, especially if the war drags on or, worse, if it escalates. The only positive point to emerge from the war is the acceptance of the need for greater collaboration across Europe on issues of common interest or concern, as in this case. Such collaboration would greatly contribute to effectively tackling climate change and possibly resulting in joint action programmes between the EU and non-EU European countries which, up to now, have been lacking or not ambitious enough. Joint action programmes should also cover energy policy in Europe.

That said, collaboration within and between European countries needs to be based on effective political (between countries) and social dialogue (within countries). Collaboration across the EU is, as might be expected, more structured and there are varying levels of engagement with both public and private investments and accompanying economic and social policies aimed at supporting the transition. Besides, there are different underlying social and economic conditions. Outside the EU, however, the level of commitment, whether political or socio-economic, differs considerably, lacking a coherent, structured approach other than the general commitment to the Paris Agreement.

There is also another fundamental difference. The commitment to social dialogue is not as strong in a number of non-EU European countries as it is within the EU. This is deemed to be highly relevant given that social dialogue can lead to better designed accompanying policies to address climate change. The Council of Europe could fill the vacuum in this regard by being the vehicle to drive forward a coordinated transition policy among the non-EU European countries, as well as acting as the catalyst for closer collaboration between the EU and non-EU European countries.

The Council of Europe has both credibility and standing with the European institutions and is ideally placed to act as a mediator between the EU and its Member States and the rest of Europe on a matter that impacts all European countries.

It is also important to note the role of the Council of Europe Development Bank (CEB), which can provide financing and technical expertise for projects with a high social impact in its member states. Such projects can support social cohesion and strengthen social integration in Europe.[13]

As outlined on its portal, the CEB contributes to the implementation of socially oriented investment projects through three sectoral lines of action, namely:

Inclusive growth: working to guarantee access to economic opportunities to ensure a prosperous future for all.

Support for vulnerable groups: helping to integrate the most vulnerable citizens to nurture a more diverse society.

Environmental sustainability: supporting a liveable society that promotes environmental sustainability, mitigates and adapts to climate change.

The CEB, furthermore, offers various financing arrangements that allow flexibility to its borrowers and best address their needs.[14] Such financing arrangements could provide members with additional financial resources to help fund projects supporting the green transition while, at the same time, promoting social cohesion at a time of change.

Other international institutions, such as the International Labour Organization (ILO) and the Organisation for Economic Co-operation and Development (OECD), already play some role in shaping policies in both the EU and in the rest of Europe, but their role could also be important in helping to strengthen the institutional framework that European countries need to facilitate the transition.

4. Social dialogue as good practice

Within the EU, the promotion of social dialogue is enshrined in the Treaty on the Functioning of the EU. The 2016 “A new start for social dialogue” publication recognised the importance of social dialogue for recovery and competitiveness, and there can be no doubt that a profound transformation such as the green transition requires effective social dialogue. Social dialogue is an essential feature in industrial relations in a number of European countries, including in a number of non-EU states. Examples of good practice in social dialogue exist in both the EU and the rest of Europe. An example that stands out in non-EU states is that of Norway. In Norway, civil society is heavily involved in the renewal of the welfare state.[15] Civil society and grassroot

[13] https://coebank.org/en/about/mission/

[14] The CEB Project Loans usually finance predefined individual infrastructure investments while Programme Loans are used for funding multi-project programmes and are often disbursed via the CEB’s commercial bank partners. While the EU Co-financing Facility (ECF) allows for co-financing and/or *ex-ante* financing of EU-funded investment activities at the country level, the Public Sector Financing Facility (PFF) covers temporary financing gaps in the public sector and facilitates the continuation of investments and reform programmes. Lastly, the Cross-Sectoral Loan Programme (CSL) responds to the public authorities’ social infrastructure needs in several overlapping sectors.

[15] Loga, J. *Civil society and the welfare state in Norway – historical relations and future roles*, Community Development Journal, Volume 53, Issue 3, July 2018, pp. 574–591.

initiatives and organisations played a central role in the origin of the welfare state, but gradually the role of civil society in the social field decreased. In Norway, there is still a high level of civic participation, with engagement strong in the fields of culture and leisure, especially in children's leisure activities in local communities. In current public debates in Norway, as in many other European countries, the potential roles of civil society in the welfare state have been high on the agenda.

The process involves carrying out diagnostic studies, such as white papers and official reports involving civil society at all levels (those organisations that are represented in official institutions and those that are not, such as NGOs representing communities in remote regions or disabled persons and other vulnerable groups). Civil society is seen as an important resource for promoting the welfare and social innovation, as well as entrepreneurship based on societal values.

The example of Norway should be compared with the degree of involvement of civil society in other countries in promoting the welfare and safeguarding the interests of low-income households and vulnerable groups. The situation is not the same across Europe where, in a number of cases, civil society, including NGOs, is not as involved in policy participation.

Nevertheless, it should be stressed that developing welfare policies is dependent on certain economic preconditions prevailing. Likewise, the appropriate structural preconditions need to be in place to enable social innovation and the protection of vulnerable groups in a transition phase – such as in the context of the green transition – and (where possible) new collaborative relations between civil society and the welfare state.

Social dialogue has proven its positive contribution to successful restructuring in a number of economies, and evidence shows that companies with well-functioning social dialogue perform better, are more resilient and pay higher wages. It should also be emphasised that all levels of social dialogue at European, national, sectoral, regional and plant level, have crucial but distinct functions in managing and facilitating the green transition. However, structures and institutions at these levels have very different strengths.

Institutions may lack the resources to formulate effective recommendations based on insight and analysis. Also, some organisations, particularly non-governmental organisations (NGOs) working closely with beneficiary communities, may not be represented in fora or institutions representing civil society. Such NGOs are more likely to provide an in-depth and accurate assessment of the impacts of the green transition than organisations, such as trade unions, which may be well-represented in institutions representing civil society but may not necessarily work closely with vulnerable groups in society. Giving a voice to NGOs working with communities is vital if the challenges to be faced by low-income households and vulnerable groups during the transition are to be addressed.

Social dialogue institutions and actors may also have very different levels of capacity and influence across EU Member States and across non-EU European countries, and austerity measures in the wake of the 2009 financial crisis have actively contributed to their weakening. Social injustice and inequality increased dramatically in several European countries during the financial crisis, thereby weakening the role of civil society.[16] Austerity measures were not administered in a balanced manner, hitting the poorest members of society hardest. Such an approach must be avoided at all costs across Europe, if accompanying policies to support the

[16] https://www.politico.eu/article/austerity-measures-have-increased-social-injustice-and-inequality/

green transition are to effectively target low-income and vulnerable groups during the transition. Clearly, the social dimension, and social policy specifically, must be given priority during the green transition, while the social dialogue structures will need to be actively supported and strengthened.

Where these structures are weak, it will be important to implement policies and measures that have been carefully designed following consultations with the social partners, as was the case with the EU's Recovery and Resilience Facility.[17] The relevance of involving social partners in policy-making was highlighted at a joint ILO-EC Conference held in 2020 entitled "Enhancing social partners' and social dialogue's roles in a changing world of work". The objective of this conference was to examine how the social partners in 34 European countries are adapting to the upheavals in the world of work, driven by technological innovation, demographic shifts, climate change and globalisation. The conference analysed and documented how the social partners in European countries are endeavouring to adapt to changes such as climate change and the challenges they have faced in adapting. The conference also sought to list the many good practices of social dialogue emerging in various countries, as well as identify the action taken by public authorities to enhance the role of social dialogue, including collective bargaining, in tackling the new challenges and opportunities in the new world of work, while at the same time promoting the autonomy of the social partners.

The conclusions of the conference identified three main priorities: (i) strengthen the social partners' representativeness and increase their institutional capacity to shape labour markets through social dialogue and consultative processes; (ii) strengthen the autonomy of the social partners who are concerned that there is insufficient room left to develop autonomous social dialogue, notably because of excessive intervention by the state, including the proliferation of legislation; and (iii) the need for an overall social partners' strategy specifically in regard to establishing an institutional framework that allows for autonomy and facilitates the effectiveness of the social dialogue institutions in terms of results.

In the EU, the participation of organised civil society in the implementation phase of the National Recovery and Resilience Plans (NRRPs) aimed at supporting economic recovery and, indirectly, the green transition in the aftermath of COVID-19, took place in different forms. The information provided by social partners identified four categories of involvement: (1) statutory; (2) through special NRRP working groups; (3) through stakeholder meetings; or (4) no specific form of involvement planned.[18] This is not to say that participation of organised civil society was always effective and structured and, despite the European Commission stressing the importance of stakeholders' engagement in the process, this was not the case in all Member States. Nevertheless, there is no question of the importance of effectively involving organised civil society during the formulation of the NRRPs, and this should apply to similar initiatives across Europe.

In this regard, a Business Europe survey conducted in early 2022 showed that the social partners were increasingly involved in the recovery plans. This is reflected in a dissatisfaction rate of only 30% regarding their role so far in the implementation of the plan, compared to 71% the previous

[17] The aim of the Recovery and Resilience Facility is to mitigate the economic and social impact of the coronavirus pandemic and make European economies and societies more sustainable, resilient, and better prepared for the challenges and opportunities of the green and digital transitions.
[18] DRAFT RESOLUTION, European Economic and Social Committee: Involvement of Organised Civil Society in the National Recovery and Resilience Plans – How can we improve it?

year regarding their role in the design of the plan.[19] Besides, as underlined in Eurofound's report of March 2022, following the adoption of the plans, the social partners stressed the importance of the country reports issued by the European Commission in the context of the European Semester. These reports framed the discussion on the implementation of national reforms and investments, allowing the social partners to exchange ideas and contribute to the NRRPs using a sound baseline.[20]

It should be stressed that social dialogue is rooted in the history of the European continent, and this distinguishes Europe from most other regions of the world. However, as mentioned earlier, the level of involvement of social partners in decision making varies from country to country and, in some countries, the level of involvement is either token or virtually non-existent.[21] This runs counter to the International Labour Organization's Centenary Declaration for the Future of Work which emphasises that social dialogue, including collective bargaining and tripartite cooperation, contributes to successful policy and decision-making. The Resolution adopted by the International Labour Conference in June 2018 underlined that social dialogue and tripartism are essential for democracy and good governance.[22]

5. Employment effects of transition

The relevance of social dialogue cannot be overstated. It can facilitate a just transition that takes into account both the employment and distributional effects of a shift to a net zero economy. It can also help to put into place a policy framework such as the "Fit for 55" package (as in the EU) providing for corrective measures supplementing those proposed to achieve climate neutrality. These issues span many dimensions, such as the distributional effects of decarbonisation policies, job losses and employment transitions, the protection of fundamental social rights enshrined in the European Social Charter and the inclusion of citizens and organised civil society in decision-making.

As discussed earlier, the Just Transition Fund and the Social Climate Fund proposed as part of the "Fit for 55" package, are some of the main EU measures announced to date which aim to mitigate the impact of the transition on the most affected regions, vulnerable individuals and businesses.

It should be noted that the European Commission has also proposed a non-binding Council Recommendation to ensure a fair transition towards climate neutrality, and to provide guidance to Member States on how to tackle the social and employment effects of the transition. These include:

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[19] https://www.businesseurope.eu/publications/businesseurope-reform-barometer-2022-taking-stock-eus-competitiveness-after-2-years

[20] Eurofound, *Involvement of social partners in the national recovery and resilience plans* (europa.eu).

[21] Ghellab, Y and Vaughan-Whitehead, D *Enhancing social partners' and social dialogue's roles and capacity in the new world of work – overview*, International Labour Organisation (2020). https://remplatestst.ilo.org/wcmsp5/groups/public/---ed_protect/---protrav/---travail/documents/event/wcms_738470.pdf.

[22] ILO, Resolution concerning the second recurrent discussion on social dialogue and tripartism, adopted by the ILC at its 107th session, June 2018, https://www.ilo.org/ilc/ILCSessions/previous-sessions/107/reports/texts-adopted/WCMS_633143/lang-- en/index.htm

- Demonstrating how the job creation potential of the transition hinges both on the active support to labour market transitions and job creation, and on the ability of workers to obtain a skillset adapted to a labour market and industrial landscape characterised by green jobs and climate-friendly production processes.[23]

- Providing modelling evidence for the ability to shift tax revenues away from labour to climate-related revenue generation, to internalise negative environmental externalities by promoting the 'polluter pays principle' and improve labour market outcomes while lowering exposure to environmental hazards, not least for the most vulnerable, as well as the ability to mitigate adverse distributional effects through targeted measures transferring back revenues from energy taxes and carbon pricing to the most affected households, in particular vulnerable ones.

- Underlining how dedicated investments in energy efficiency, decarbonisation of heating, cooling and transport, access to essential services, including alternative sustainable mobility solutions, and awareness raising, complemented where necessary with temporary and targeted direct income support for vulnerable consumers and households, can ensure a fair and inclusive energy transition, with a focus on the most affected people and households, in particular vulnerable ones.[24]

This is all laudable, but the transition challenge is formidable, and the risks to existing jobs are real as claimed by trade unions who have warned about deepening economic and social divisions between eastern and western EU countries caused by the EU's 2050 climate neutrality goal.[25] Trade unions are particularly worried about the social and economic divisions that the Green Deal agenda risks creating between poorer eastern EU countries like Poland, Bulgaria and Romania (where employment in some regions can be entirely dependent on a single, heavily-polluting industry) and their richer western neighbours. The situation is more acute in most non-EU European countries, namely the Balkan states, eastern European countries and Russia where the dependency on carbon-intensive industries is more prevalent. This presents a huge challenge for these countries, be they in the EU or otherwise, and it is no surprise that trade unions in the Czech Republic expressed serious misgivings about the green transition and its impact on jobs in the car manufacturing industry where non-electric powered vehicles are produced.[26]

The situation also requires a policy response to expand economic opportunities in countries and regions where the transition is expected to lead to job losses. This too presents a huge challenge with the transition possibly likely to have a twin effect: workers on one side and low-income households and vulnerable groups, including migrants resident in European countries, on the other. Supply-side policies should ideally be applied to create new jobs along with specific interventions aimed at marginalised groups.

Supply-side measures to create new jobs are of paramount importance, along with specific interventions aimed at low-income households to facilitate access to decently remunerated jobs, supplemented by policies favouring development in remote areas. These measures will clearly require public investments to support the green transition. Also, a renewed commitment in

[23] This was true for all previous transitions, but they are still very relevant.
[24] European Commission Proposal for a Council Recommendation on ensuring fair transition towards climate neutrality (2021).
[25] https://www.euractiv.com/section/energy-environment/news/eleven-million-jobs-at-risk-from-eu-green-deal-trade-unions-warn/
[26] These concerns were expressed during a conference organised by the Workers' Group of the European Economic and Social Committee in Prague on 11th October 2022.

international fora to enforce fairer trade rules while protecting labour rights as human rights is also deemed necessary.

In any event, the transition towards climate neutrality will require large-scale restructuring, especially in the manufacturing, transport and construction sectors. That will impact tens of millions of jobs across Europe, and has to happen in a balanced, managed and forward-looking way.

Article 1 of the European Social Charter provides for the right to work: everyone shall have the opportunity to earn his living in an occupation freely entered upon. By accepting Article 1§1 of the Charter, States Parties undertake to pursue a policy of full employment.[27] For this purpose, States must adopt and follow an economic policy which is conducive to creating and preserving jobs and they must take adequate measures to assist the unemployed in finding and/or qualifying for a job.[28] Labour market measures should be targeted, effective and regularly monitored.[29] Such measures should also be designed to support migrants, refugees and internally displaced persons entering the labour market, as well as minorities with distinct levels of under-employment or unemployment (especially Roma).[30]

As already stated, all of this requires effective social dialogue at both the macro and micro levels. In the EU (assuming the funds made available are adequate), the Just Transition Fund can be considered as an important financial instrument to support workers in their transition to new jobs. However, and as has been argued by the European Economic and Social Committee, the funds may not be sufficient to support the economic change both in terms of its resources and scope.[31] Again, in a wider European context, it appears necessary for non-EU European countries to develop a similar financial instrument, the implementation of which could possibly be coordinated by the EBRD. The question remains, however, whether the financial resources made available would adequately support the transition towards a more sustainable economy across Europe. There is also the challenge of high rates of inflation currently impacting all European countries without exception, with the cost of borrowing rising significantly after years of near or zero interest rates.

The three dimensions of sustainable development – economic, social and environmental – are closely interrelated and need to be addressed by means of a comprehensive and consistent policy framework. It should be noted that the ILO Guidelines for a just transition towards environmentally sustainable economies and societies for all provide a set of practical tools for governments and social partners to manage this transition process.

The 2015 ILO Guidelines for a just transition state that "*strong social consensus on the goal and pathways to sustainability is fundamental. Social dialogue has to be an integral part of the institutional framework for policymaking and implementation at all levels. Adequate, informed and ongoing consultation should take place with all relevant stakeholders*".[32]

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[27] Greek General Confederation of Labour (GSEE) v. Greece, Complaint No. 111/2014, decision on the merits of 23 March 2017, §125
[28] Greek General Confederation of Labour (GSEE) v. Greece, Complaint No. 111/2014, decision on the merits of 23 March 2017, §125
[29] Conclusions 2012, Albania
[30] Conclusions, 2020, Azerbaijan; Conclusions 2020, Lithuania
[31] EESC NAT/864 Social dialogue within the green transition
[32] International Labour Organisation (2015) *Guidelines for a just transition towards environmentally sustainable economies and societies for all*.

The ILO guidelines also stress the need for coherent policies across the economic, environmental, social, education/training, and labour sectors to enable businesses, investors and workers to embrace and drive the transition forward. Such a framework is crucial to addressing any negative distributional effects arising from a more sustainable economic policy where the driving force is not necessarily the measurement of economic growth. A strategic and coordinated approach is vital to implement policies successfully but *a priori* this requires both a macro and micro analysis of the economy and of society too as it transitions towards a more sustainable economy. Earlier, reference was made to the relevance of social dialogue and the role it plays in crafting policies that facilitate change and reform. A strategic and coordinated approach needs social dialogue, including at the stage of how the transition can be funded by way of, for example, environmental taxation or redistribution policies. Such an approach, therefore, would facilitate both the transition and support social cohesion in this period of transition.

The objective of coordinated and coherent policies is of course climate neutrality since, without it, there is no social cohesion, wealth creation or improvements to the quality of life — the overall logic behind climate neutrality. However, these policies also need to be supported by a just transition framework for all in order to promote the creation of better paid jobs. This has to happen while anticipating the impacts of the transition on jobs, particularly those that are most threatened by the development of new, more sustainable infrastructure in, for example, the transport, energy and manufacturing sectors.

The ILO also calls for more adequate and sustainable social protection for job losses and displacement during the transition. This will of course require substantial financial resources. However, this cannot be taken for granted given the current situation with the financial pressures arising from European governments providing support to households and businesses because of rising energy prices. The current crisis could possibly derail climate change targets if its effects drag on.

Another relevant aspect is how wealth distribution and tax reform proceed in support of the transition and are targeted at those sectors affected negatively by the transition. Making sure that measures are targeted will require the consensus of organised civil society as argued above. Included in the targeted measures are relevant education and re-training programmes with a heavy information technology focus.

Importantly, targeted policies and related measures must recognise that there is no “one size fits all” solution. As stated in the ILO guidelines, policies and programmes need to be designed in line with the specific characteristics of countries, including their stage of development, economic sectors, and the types and sizes of enterprises. This is often taken for granted, and impact assessments carried out by the European Commission are essentially macro- rather than micro-oriented. A good example is the Commission’s proposal on the next generation of EU own resources.[33] The proposed new sources of revenue will help repay the grants element of the NextGenerationEU (NGEU) economic recovery instrument that the European Commission, on behalf of the EU, is financing *via* capital markets funding. The new own resources should also

[33] The European Commission has proposed establishing the next generation of own resources for the EU budget by means of three new sources of revenue: the first based on revenues from emissions trading (ETS), the second drawing on the resources generated by the proposed EU carbon border adjustment mechanism, and the third based on the share of residual profits from multinationals that will be re-allocated to EU Member States under the recent OECD/G20 agreement on a re-allocation of taxing rights (“Pillar One”).

finance the Social Climate Fund, designed (in theory) to make sure the transition to a low-carbon economy leaves no one behind.

6. Additional burdens of the transition

The new own resources will help to repay the funds raised by the EU to finance the grant component of NGEU. They should also finance the Social Climate Fund *via* the "Fit for 55" package. While the three new sources of revenue, as proposed by the Commission, provide a sensible way forward, caution should be exercised about any impact the additional revenue could have on consumers and vulnerable groups. If an increase in the tax burden is unavoidable, then this must be accompanied by a tax reform, or the introduction of compensatory mechanisms at national level, or a combination of the two.[34] In this connection, a recent study conducted by Ecorys on behalf of the European Commission[35] looked at the economic literature on taxation in support of the transition. The study drew up an inventory of tax measures consisting of taxes and tax incentives and developed a benchmarking methodology to assess the measures analysed. Ten measures were selected as examples of good practice, in view of their overall environmental effectiveness and political viability (including economic and distributional implications). The selection also reflected the diversity of types of measures.

The research shows that environmental taxes and beneficial tax incentives are tools increasingly used by countries to support a green transition towards lower GHG emissions. The study also identified more than 260 taxes and tax incentives that fell within the scope of the research approach.

A growing body of research is therefore available to countries. This can help them to make informed policy choices, striking a successful balance between designing tax measures that are effective in reducing GHG emissions and yet reflecting the wider policy implications. At the same time, the research also highlights that there is still room for countries to improve and learn from each other. Although there is a growing body of evidence that could help to design taxes more effectively, in many instances, countries still resort to second-best or less effective schemes. In addition, there are still important gaps in the research, especially with regard to tax incentives.

This raises doubts as to what extent policy makers can resort to solid empirical evidence when designing specific measures. The work on the inventory of tax measures highlighted that the availability of *ex post* evaluations, particularly of tax incentives, is limited. However, this information is crucial to support administrations that are considering greening their tax schemes. Countries also need to reflect on whether there is room to enhance their efforts to curb GHG emissions *via* taxation. In some instances, the design of measures might serve other purposes, including revenue generation or meeting political demands, rather than focusing on reducing emissions. The study concludes that striking the right balance between diverse and often conflicting interests will remain a huge challenge for future policy making.

Indeed, this is the main issue to contend with in tax reform, along with providing compensatory measures to mitigate negative effects arising from the green transition. Adopting a stick and carrot approach may be the desired way forward with green taxes on harmful environmental activities,

[34] P. Von Brockdorff, ECO/561, *Proposal for an own resources decision*
[35] https://www.ecorys.com/belgium/our-work/taxation-support-green-transition-overview-and-assessment-existing-tax-practices

and tighter regulations representing the stick; on the other hand, compliance with new environmental standards and certifications for energy performance, emissions and pollutants would give rise to tax reductions. Such schemes would serve as carrots, along with low-interest loans and grants for green investments in sustainable agriculture, renewable or low-carbon energy sources, energy-efficient buildings, public walkways and cycle paths and electric vehicle (EV) infrastructure.

Subsidies and tax rebates are additional tools to boost demand for green products and services like EVs, solar panels or renewable energy. Governments may also offer subsidies and grant funding to research institutes, academic institutions and private R&D firms to boost innovation and develop transformative technologies in areas such as renewable energy, carbon capture, waste management, and energy efficiency. Above all, governments would need to compensate low-income households and vulnerable groups. These measures would need to be targeted and compensate for additional transport or energy costs induced by the transition.

The report referred to in Footnote 34 also refers to the financing of the EU's Social Climate Fund. This Fund will ensure a socially fair transition and support vulnerable households, transport users and micro-enterprises by financing investments in energy efficiency, the installation of new heating and cooling systems, and cleaner mobility. If necessary, temporary direct income support may also be provided.

Another relevant consideration highlighted in the report is that the financial burden of the proposals must be fairly distributed among the EU Member States. In this context, the report refers to the structural differences among Member States, giving rise to varying impacts from the transition.

According to the ILO Guidelines, governments should, in consultation with social partners:

(*a) encourage sound labour market policies that help enterprises and workers in the anticipation of changing labour market demands in the context of the transition to environmentally sustainable economies by facilitating access to jobs, strengthening employability and training;*

(b) give particular attention to unemployed workers and workers at risk of unemployment in communities and industries affected by climate change, resource degradation or structural change including those in the informal economy;

(c) promote an efficient and effective delivery of employment services that respond to the needs of enterprises and workers in the transition to environmentally sustainable economies and extends outreach to those outside of the formal labour market;

(d) develop and support, through public and private employment service providers, tailor-made courses directly linked to specific occupations and entrepreneurship opportunities in the green economy;

(e) adapt and strengthen public employment services to further develop their role as transition agents. They should provide information, guidance, matching services and training. These services can be improved by expanding innovative ways of reaching out to jobseekers;

(f) consider supporting public works and employment programmes, including initiatives linking poverty eradication and ecosystem protection, as well as those for workers affected by the

transitioning to environmentally sustainable economies including climate change, who have been laid off due to structural or technological change; and

(g) consider introducing active employment policies including, among others, well targeted subsidies that allow workers to access education and acquire skills that improve their employability through work experience and on-the-job training.

The above measures would help mitigate the financial burden for those individuals and households who would be impacted by the transition. They could be deployed in all European countries, although this may present a huge challenge if civil society has little or no say in shaping labour market policies and if there is no commitment on the part of governments for active labour market policies. The aforementioned report also welcomes how the EU's Social Climate Fund will be allocated nationally, based on the relative wealth on a country-by-country and region-by-region basis. However, the report emphasises that fairness in the way the proposals are implemented across the EU is absolutely essential, with differences at the level of each country and region, particularly in terms of carbon-intensive industries, taken into account.

This is particularly relevant since the impact of the transition and the application of policy instruments, such as those mentioned above, on countries (and this obviously applies across Europe) and households will vary depending on the level of development in the case of each country, as well as the level of household income. In the latter case, it will also depend on supplementary income or in-kind transfers received by the household in question *via* social security or *ad hoc* support measures targeting low-income households or vulnerable groups.

The distributional effects of, for example, carbon pricing (to reduce the level of emissions) needs to be assessed well before this policy is applied widely across Europe. This can be explained with reference to, for instance, the European Commission's proposal for a new generation of own resources aimed at generating funds to finance the NextGenerationEU and the Social Climate Fund. The proposal to shift the Emissions Trading Scheme revenues from being essentially a national resource to an own resource is necessary to generate funds, as explained above. However, the challenge here remains that of how such revenues would be re-invested in a way that would be beneficial for communities, with low-income households and vulnerable groups benefitting the most. Ideally, the impact of this proposal on sectors such as the property market needs to be assessed on a country-by-country or region-by-region basis, as planning rules vary and the cost of energy efficiency could lead to higher property prices impacting especially low- to middle-income earners.

It should be stressed that the effect of the transition on housing must feature prominently in the list of measures aimed at mitigating the impacts.[36] The European Social Charter stipulates that States Parties must guarantee to everyone the right to adequate housing.[37] They should promote access to housing in particular to different groups of vulnerable persons, such as low-income persons, unemployed persons, single parent households, young persons, persons with disabilities including those with mental health problems.[38]

In this context, the EU's NextGenerationEU also aims at embracing the green and digital transitions whilst focusing on restoring the social fabric. The Just Transition Fund – and in the first

[36] https://www.euractiv.com/section/energy/opinion/housings-role-in-europes-green-transition/
[37] Conclusions 2003, France
[38] Conclusions 2003, Italy

place, measures focusing on housing renovation – could also contribute to improving living conditions and combating poverty through carefully calibrated and targeted measures, reconciling social objectives and climate change mitigation goals.

The strengthening of the Just Transition Fund, through an additional €32.5 billion of funding from the recovery package, as well as an additional €10 billion from the 2021-27 budget and €10 billion in loans from the European Investment Bank, is aiming to make at least €150 billion available for investments in the just transition. The increase in funding is not only a necessity but also presents an opportunity: public investments in the recovery will also have to include measures aimed at improving people's living conditions: financing of the supply of affordable housing must be an integral part of the process.

The final point in regard to the emission trading system proposal is the inclusion of a temporary solidarity adjustment mechanism, which helps to ensure a fair own resource contribution from all Member States, with an upper and lower limit applied in relation to the gross national income key. This will prevent some Member States from contributing disproportionally to the EU budget relative to the size of their economy, as Member States transition towards more sustainable economies.

Clearly, the EU is quite creative in designing solidarity measures to support social cohesion and reduce inequality. Nevertheless, inequality in the EU remains an issue. In fact, inequalities have increased in some countries in recent decades, due to factors such as globalisation, technological change, taxation policy and the economic crisis. These inequalities are hampering economic growth and can lead to social conflict, reducing participation in society and leading to increased social exclusion.[39]

In response, the EU decided in 2017 to put into place the European Pillar of Social Rights, which makes a direct reference to the European Social Charter as a tool providing a complete set of social rights. It aims at tackling inequalities in key areas and thereby strengthening the European social model. The main components of the Pillar are equal opportunities and access to the labour market, fair working conditions, adequate social protection and social inclusion. The European Social Charter extends these objectives across Europe, including to non-EU countries, even if implementation could further be developed. Nevertheless, and as already pointed out, the funding required to support the transition in non-EU European countries urgently needs to be addressed, including whether funding should be conditional on the respect of social and fundamental rights.

7. Effects of transition between and within countries

Against this background, two key aspects need to be considered with regard to the distributional effects of the transition towards climate neutrality and the application of a higher rate of carbon pricing. First, one needs to consider the effects between European countries and second, within countries.

In the context of the EU, this would also necessitate an assessment of the proposed Carbon Border Adjustment Mechanism (CBAM) aimed at reducing the risk of carbon leakage into the EU

[39] https://www.eurofound.europa.eu/topic/inequality

by putting a carbon price on imports, corresponding to what would have been paid had the goods been produced in the EU. This mechanism will apply to a targeted selection of sectors and has been deemed by the European Commission to be fully consistent with the WTO rules.

The CBAM has a symmetric component, meaning that it would be applied symmetrically to imports and exports. Goods imported to the EU would pay a charge which reflects their "carbon content" – that is the CO_2 emissions generated by their production (the charge being calculated so that the overall price of these CO_2 emissions is the same as the EU carbon price). Symmetrically, goods exported to other countries would benefit from a rebate reflecting the difference between the carbon price paid for their production in Europe and the carbon price in the destination market. A symmetrical CBAM would level the playing field between producers facing different carbon prices in the countries where their production is located. Clearly, there needs to be an assessment of the CBAM in each country as part of the process of addressing any adverse distributional effects that might arise from the application of carbon pricing in the transition phase. [40]

In assessing any likely impacts on countries and households, it is necessary to look at how each could be impacted by increased carbon pricing focusing on both the supply and demand side of the equation.[41]

In terms of supply, there is no question that the cost of the investment necessary to meet the targets set by the EU, or the Paris Agreement in the case of non-EU European countries, will vary considerably, further complicated by the high inflation rates being experienced at present.

However, some countries will also find it less challenging to transition towards a climate-neutral economy given that there is already either a significant investment in renewable energy and sustainable transport, or the scrapping of old polluting installations is already underway. It should also be noted that the emission profiles of countries differ and, in a number of cases, significantly, with some countries having more emissions in sectors that are relatively cheap to decarbonise. Examples of this are old polluting installations, including power plants, which are expected to close anyway. Thus, the cost of reducing emissions in such cases would be lower than in more recent installations with much higher residual values.

As far as households are concerned, they could also be impacted by supply-side factors such as changes in the labour market, income or support transfers, as well as capital income as economies transition towards carbon neutrality. These changes will affect household groups differently. Whereas high-income and to a lesser extent middle-income earners would be expected to cope with the possible additional costs of living arising from the transition, the same cannot be said for low-income households and vulnerable groups who rely on fixed incomes and who will inevitably require income support during the transition.

In terms of demand, there are clear differences across countries with regard to *per capita* incomes both at national and regional level, with a higher carbon price expected to place an increased burden on poorer households relative to national consumption expenditure. The increase in carbon pricing is also expected to have an uneven impact of carbon price-induced changes in

[40] P. Von Brockdorff, ECO/561, *Proposal for an own resources decision*

[41] See Gustav Fredriksson and Georg Zachmann, Ottmar Edenhofer, Matthias Kalkuhl and Christina Roolfs, Karen Pittel, Don Fullerton, Jan Christoph Steckel, Sebastian Renner and Leonard Missbach, *Winners and Losers of Energy and Climate Policy – How Can the Costs Be Redistributed?*, CESIFO Forum, 2021.

consumption prices across households. Carbon pricing will inevitably make emissions-intensive goods and services, such as petrol and heating fuels, more expensive compared to goods and services with lower carbon content. This has an uneven impact across households since their expenditure patterns differ. Poorer households typically spend a larger share of their income on energy goods, meaning their consumption will become relatively more costly. A carbon price or an upward adjustment in carbon prices will therefore hit poorer households harder than middle- or high-income households. Hence, the logic behind targeted income support and compensatory measures.

In a study referred to in Footnote 41, the authors assessed the distributional effects arising from increased carbon pricing between countries. It is clear that to meet either the targets set by the EU, or the Paris Agreement for other European countries, it is necessary to consider the inter-country distributional effects of meeting the higher abatement through carbon pricing. To simplify the analysis, the authors assumed a single uniform carbon price, covering all sectors and countries in the EU, increasing over time to meet the EU's targets.

The higher carbon price will obviously induce abatement by countries and, as explained earlier, some countries will find it cheaper than others to reduce emissions. As the authors explain, part of the reason is that abatement opportunities differ within a given sector. Some Member States can, for instance, still close polluting installations that have exceeded their economic lifetime, while others will have to make significant additional investments to reduce emissions within the same sector. However, there are also differences in abatement opportunities across sectors.

EU Member States with a relatively high level of industrialisation have a high share of industrial emissions which are costly to abate, while less industrialised Member States generally emit relatively more in their power sectors, and these emissions are often cheaper to reduce. In view of this difference, the authors conclude that some countries will find a given carbon price more challenging than others since the carbon cost will constitute a higher share of their national consumption expenditure. *Households in Poland (per-capita emissions of 10.4 tonnes), for instance, will on average find a carbon price of €60 more burdensome than German households (per-capita emissions of 10.1 tonnes) relative to their consumption expenditure (actual individual consumption per capita in Poland in 2020 was less than €9,000 and in Germany almost €23,000).*

On average, therefore, poorer EU Member States are likely to be more impacted by the transition towards carbon neutrality than more industrialised ones, and this argument can safely be extended to other European countries outside the EU. There are, therefore, clear distributional implications between countries, but also within countries, with the authors using expenditure and income-side analysis to determine the distributional effects of the transition.

In terms of expenditure, higher carbon pricing will make emissions-intensive goods and services, such as fuel and heating or cooling, more expensive compared to goods and services with lower carbon content. The effect of this across households will be uneven since their expenditure patterns differ. Typically, low-income households spend a larger share of their income on energy goods, meaning their consumption becomes relatively more costly. An increase in the carbon price, therefore, has a heavier impact on the consumption expenditure of poorer households.

There is also the income effect to consider with households being impacted by rising fuel and energy prices, as well as the secondary effects of higher fuel and energy prices which would almost inevitably include higher prices for day-to-day consumption of goods and services. There are actually two effects to consider: the income and the substitution effects. Both are components of the price effect (that is, the decrease in quantity demanded of a product due to an increase in its price). The income effect arises because a price change alters a consumer's real income and the substitution effect occurs when consumers opt for the product's substitutes. In the case of poorer households, this could lead to such households buying inferior goods to the ones they already purchase. Such a development would require a policy response to avoid these substitution effects from gaining traction as it would inevitably result in a lower quality of life for poorer households, as well as possible health effects resulting from the consumption of low-quality or unhealthy foods.

Nevertheless, it should be recalled that low-income households earn relatively more transfer income, which is less affected by carbon pricing, especially if the transfers are indexed to inflation. In contrast, households with a high level of income are likely to pay more both in absolute and relative terms. This is because they derive larger income shares from capital and labour, the returns of which would be expected to fall with higher carbon pricing.

What this means is that low-income households can be better shielded from the effects of higher carbon pricing assuming (i) tax policies are and remain progressive (ii) adequate income transfers based on a progressive tax policy are applied; and (iii) wages are inflation-indexed through wider collective bargaining coverage. There are both pros and cons with respect to a progressive system of taxation, but one cannot envisage a policy shift in the context of a green transition or any context for that matter, especially where the interests of the poorest households in a society are prioritised. The same argument holds for income transfers the objective of which is to support poorer households at any time and especially during times of financial stress or transition.

Wage indexation is also meant to support households when prices of goods and services rise. Simply put, wage indexation is the automatic adjustment of wage and pension amounts based on fluctuations in the prices of consumer goods and services. With wage indexation, purchasing power is not lost due to inflation. Indexation, therefore, acts as a buffer against inflation for households especially for poorer households who in the absence of indexation would not be able to afford essential commodities. Employers are never enthusiastic about wage indexation because it implies higher costs independent of the bottom line. That said, wage indexation, which is a point of contention in collective bargaining,[42] helps to protect real incomes also in a transition as big as the green transition.

The Hayekians[43] would of course argue against progressive taxation and wage indexation stating that both would run counter to rewarding economic effort and investment. There may be some truth in that, but Europe has, over the years, sought to pursue a social market economy and, if anything, European institutions, such as the European Commission, the European Parliament and the Council of Europe, should ensure that members of either the EU or the Council of Europe

[42] Article 6 of the European Social Charter stipulates that All workers and employers have the right to bargain collectively. The exercise of the right to bargain collectively and the right to collective action, guaranteed by Article 6§2 and 6§4 of the Charter, represents an essential basis for the fulfilment of other fundamental rights guaranteed by the Charter, including for example those relating to just conditions of work (Article 2), safe and healthy working conditions (Article 3),fair remuneration (Article 4), information and consultation (Article 21), participation in the determination and improvement of the working conditions and working environment (Article 22), protection in cases of termination of employment (Article 24), protection of the workers' claims in the event of the insolvency of their employer (Article 25), dignity at work (Article 26), workers' representatives protection in the undertaking and facilities to be accorded to them (Article 28), information and consultation in collective redundancy procedures (Article 29).

[43] The Hayekians is a student group at the University of Chicago dedicated to the discussion of libertarian ideas and policies.

apply this model as faithfully as possible. This is a formidable challenge given that, in some EU Member States and more so in non-EU European countries, civil society representation and collective bargaining coverage remains relatively low.

Of particular significance in the EU context is the EU's directive on adequate minimum wages.[44] The directive highlights the importance of collective bargaining for wage setting as an important tool to ensure that workers can benefit from adequate minimum wages. The directive also aims to extend the coverage of workers through collective bargaining. That is why the EU co-legislators agreed that Member States should promote strengthening the capacity of social partners to engage in collective bargaining, including the protection of workers' representatives.

It should be recalled that, across the EU, Member States differ widely in terms of workers' coverage by collective agreements and minimum wage levels. This is in part due to the very different labour market models and different income levels in the Member States.

The directive on adequate minimum wages aims to help to achieve decent working and living conditions for employees in Europe by placing emphasis on fair working conditions, that is, workers having the right to fair wages that provide for a decent standard of living. This is outlined under principle 6 of the European Pillar of Social Rights.[45] As mentioned earlier, the European Pillar of Social Rights is a joint proclamation by the heads of the EU institutions, committing to implementing 20 principles in the area of social policy. Underlying these principles are social dialogue and the involvement of workers' representatives on matters relevant to workers, including matters such as wage indexation. This is principle 8 of the European Pillar of Social Rights. Also, as pointed out earlier, the Council of Europe could take a leading role by reinforcing the European Social Charter mechanism, which provides a similar framework for non-EU European countries.[46]

Evidence suggests that indexing wages, as well as transfers (such as pensions) can shield poorer households and help compensate low-income households for higher consumption prices caused by carbon pricing.[47] This needs to be considered in any policy or measure aimed at mitigating the impact of higher carbon pricing. Thus, assuming transfers to low-income households are inflation-indexed, complementary or targeted support measures must be crafted in line with this method.

Nevertheless, indexation (wage or price) can produce mixed results.[48] In economies affected by economic shocks, indexation may destabilise output and create inflationary momentum. It may also cause some deterioration in the equality of income distribution during periods of economic reform. On the other hand, indexation may help to stabilise monetary conditions, especially in the face of shocks impacting the business cycle.

It may also help to increase the political sustainability of adjustment and stabilisation policies, if indexation is seen as a signal of government concern for the welfare of low-income earners. This

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[44] https://www.consilium.europa.eu/en/policies/adequate-minimum-wages/

[45] https://ec.europa.eu/info/strategy/priorities-2019-2024/economy-works-people/jobs-growth-and-investment/european-pillar-social-rights_en

[46] See Preamble of B. Revised Social Charter of 1996: "…the Member States of the Council of Europe agreed to secure to their populations the social rights specified therein in order to improve their standard of living and their social well-being". Also, the Social Charter refers to the right to protection against poverty and social exclusion (Article 30). As stated in this report, low-income households and vulnerable groups need to be protected during the green transition (and exclusion avoided) otherwise there is a real risk of a further increase in income inequalities.

[47] https://www.ipe.com/weighing-up-the-benefits-of-indexation/26752.article

[48] https://documents1.worldbank.org/curated/en/557411468767378442/pdf/multi-page.pdf

last point is indeed an important consideration and one that policy-makers should keep in mind when developing indexation mechanisms to help reduce rising inequalities across Europe.

It should be noted that inequality (in terms of socio-economic conditions) has increased in Europe slowly but surely since the mid-1980s.[49] With the increased adoption of market-oriented policies in sectors such as education and health, divergences in the quality and accessibility of social services have also increased. Concerns over inequalities further surged in the aftermath of the post-2008 financial crisis, and inequalities have now reached levels where they threaten democracy in Europe. Examples include Hungary, Albania, and Bosnia and Herzegovina.

The Eurofound study referred to in Footnote 39 also identified another worrying trend: in terms of providing equal health benefits and protections to guarantee citizens' abilities to exercise their basic rights, the situation has worsened significantly in sixteen European countries (47%), while only improving in five countries (15%) and staying essentially the same in thirteen countries. The worst offenders in terms of making greater numbers of citizens unable to exercise their basic political rights because of inadequate healthcare provision are countries like Hungary, Lithuania, Macedonia, Poland, Romania, Slovenia, and Spain. The connection between political rights and heath care is particularly significant as stated in the Constitution of the World Health Organisation agreed 70 years ago: "The enjoyment of the highest attainable standard of health is one of the fundamental rights of every human being without distinction of race, religion, political belief, economic or social condition". Several decades later, these words remain as relevant as ever and are echoed in the European Social Charter, Article 11, which has been accepted by nearly all the Member States of the Council of Europe to uphold the universality and indivisibility of (all) human rights.[50]

This study provides evidence of deteriorating socio-economic conditions in a number of European countries, be they members of the EU or otherwise. It is a trend that needs to be reversed if the green transition is not to result in a further worsening in inequality across Europe. It also points to the need for increased spending on education and health which, as has been pointed out earlier, represents a huge challenge for all European countries in the current economic circumstances. Besides increased public investment, the sooner principles such as those outlined in the European Pillar of Social Rights and the European Social Charter are applied the better. This should include the application of a progressive system of taxation to protect low-income households as much as possible against the negative effects of the green transition.

[49] https://carnegieeurope.eu/2019/02/04/are-increasing-inequalities-threatening-democracy-in-europe-pub-78270

[50] The right to protection of health guaranteed in Article 11 of the Charter complements Articles 2 and 3 of the European Convention on Human Rights - as interpreted by the European Court of Human Rights - by imposing a range of positive obligations designed to secure its effective exercise. The rights relating to health embodied in the two treaties are inextricably linked, since "human dignity is the fundamental value and indeed the core of positive European human rights law – whether under the European Social Charter or under the European Convention of Human Rights - and health care is a prerequisite for the preservation of human dignity". The right to protection of health must be protected not merely theoretically, but also in fact. Implementation of the Charter requires States Parties not only to take legal action but also practical action making available the resources and the operational procedures necessary to give full effect to the rights specified therein. Respect for physical and psychological integrity is an integral part of the right to the protection of health guaranteed by Article 11.

Conclusions and recommendations

The transition towards a greener and more sustainable economy will affect European countries and households unevenly, with low-income and vulnerable groups likely to be impacted most by the change unless income support measures are put into place. What is also likely is that the effects of the green transition will impact all countries: be they poor or rich.

However, whereas some of the poorer countries could transition by implementing relatively inexpensive emission reduction options, this does not apply across the board. Richer countries also face considerable challenges because their industrial sectors still rely heavily on fossil fuels. On the other hand, households in richer countries are likely to face relatively lower increases in carbon pricing than households in poorer countries, where investment in renewable energy is still lagging behind. These considerations must be factored in when assessing the distributional impact of the transition between countries.

Within countries, the distributional effect is likely to be impacted by higher carbon pricing, but also second-round effects caused by the adjustment to carbon pricing. Inevitably, low-income and vulnerable groups will be affected by the transition, and the EU proposals for a Social Climate Fund are aimed at shielding such groups from the impact of the transition. However, and as explained earlier, the adoption of good practices aimed at averting any widening of income inequalities will also help to soften the impact.

Of fundamental importance is effective social dialogue leading to carefully designed policies and measures based on a progressive system of taxation and income transfers targeted at low-income households and vulnerable groups. Progressive tax and targeted welfare systems are in place in several European countries. The adoption and further strengthening of such policies and measures based on good practice and on fair redistribution of resources are deemed to be the way forward to avert a further widening of inequalities and social exclusion. However, the current economic climate does pose a serious challenge to several European countries with financial resources being stretched because of subsidies to mitigate some, if not all, of the effects of higher energy and commodity prices.

The main recommendations are listed below:

(i) A country by country or region by region impact assessment of the effects of the green transition provides a more accurate diagnosis of the effects and makes policy response more effective.

(ii) Targeted income support measures with an emphasis on progressive taxation are an essential component of the policy package to support the transition and to avert social exclusion by avoiding the further deepening of income inequalities.

(iii) The provision of adequate financial resources to carry out diagnostic studies and to support social programmes to shield low-income households and vulnerable groups from the effects of the green transition is critical, and this applies mainly to non-EU European countries. Possible sources of funding could be the EBRD and the CEB.

(iv) Social dialogue, as well as further democratisation (in some countries, this may require substantial political changes moving in a democratic direction), are necessary to develop just transition and active labour market policies (considered crucial to support the transition) that involve social partners and NGOs in decision making.

(v) Collaboration across Europe, with the European Commission and the Council of Europe taking a leading role, is vital to maintain social cohesion during the transition. The war of aggression against Ukraine threatens to derail the commitment to a green transition. However, perhaps the one positive outcome of the war is the growing acceptance of the need for Europe to strive towards a common goal on a number of fronts, including in the transition towards a green economy.