# Chapter 9
# Targeting Portugal's Environmental Tax Incentives:
## A Comparative Look at OECD's Best Practices

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## ABSTRACT

*This paper explores the role of tax incentives within a country's fiscal policy, focusing on OECD best practices as an example of potential green fiscal measures to be implemented by Portuguese policymakers. It evaluates the effectiveness of classic Environmental Tax Reforms in addressing market failures linked to environmental degradation, while simultaneously promoting sustainable economic growth through revenue recycling mechanisms. Drawing upon the Pigouvian tax framework and the "double dividend" hypothesis, this paper provides food-for-though on the synergies between negative taxation with positive incentives, highlighting their complementary*

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*roles in fostering green innovation and investment through revenue recycling. By synthesizing theoretical groundwork with international case studies and local implementation barriers, this paper advocates for a pragmatic, incentive-compatible environmental tax system that balances ecological imperatives with economic resilience and competitiveness.*

## INTRODUCTION

Climate change and environmental degradation present existential threats to global socio-economic systems. As the world faces sequential environmental crises, policymakers are increasingly turning to green fiscal measures to steer economic behavior towards sustainability (OECD, 2019; OECD, 2025). Among these instruments, environmental taxation has gained prominence as a preferred mechanism to internalize negative externalities, particularly those related to greenhouse gas (GHG) emissions, resource overuse, and pollution. Initially rooted in the Pigouvian tradition, environmental taxes aim to correct market failures by imposing costs on activities that harm the environment, thereby aligning private behavior with socially optimal outcomes (Pigou, 1920).

Nevertheless, a growing body of literature suggests that negative taxation alone may not be sufficient to induce large-scale transformation within the scope of a broader classic Environmental Tax Reform (ETR). While negative taxation can be a useful tool, it may not be sufficient on its own, given that punitive measures introduced too early in a transformation cycle risk discouraging economic agents from committing to the very changes needed to drive meaningful progress. It is, therefore, relevant to explore the synergies between tax incentives and the already in use environmental taxes, to efficiently mitigate the economic burden of decarbonization and accelerate green technological transition. Instruments such as investment tax credits, full expense, and targeted deductions can reduce the effective cost of sustainable practices, thereby mobilizing private capital towards green infrastructure and innovation (OECD, 2025).

Portugal, like many OECD countries, has implemented some mechanisms of environmental taxation, most notably through carbon taxes and energy levies. Based on the work previously developed by *Comissão para a Reforma da Fiscalidade Verde* ("CRFV") and its recommendations, as well as learning from the international best practices related to green tax incentives in OECD countries, this paper discusses potential green fiscal measures that could be adopted by Portuguese policymakers from the Authors' understanding.

By examining theoretical models, international experiences, and Portugal's institutional trajectory, this study proposes policy pathways that reunite environmental

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