

Rule of law and its implications for the environmental taxation-income path across European Countries

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Research has clearly demonstrated that economic development is closely related to environmental quality. In last two decades this relationship has been identified by the Environmental Kuznets Curves that postulates a bell-shaped relationship between pollution and income. However, while theoretical and empirical research has focused on the polluting effects of economic development, few identified the policy instruments that can be introduced to contrast such negative effects. This paper examines how environmental taxation is related to economic development. The introduction of environmental taxes usually requires effective regulatory capabilities such as effective monitoring, enforcement and payments. We assume that these regulatory capabilities reflect the integrity of the institution of rule of law and examine how the strength of rule of law affects the environment taxation-income path. The empirical results, using data from 29 European Countries, demonstrate that the environmental taxation-income relationship is strongly influenced by the rule of law that ensures that environmental policies are implemented effectively. A strong rule of law contributes to achieving a turning point at lower levels of per capita income. Our analysis also made it possible to identify differences in environmental taxation-income paths among European countries, showing that post-transition economies may have not yet reached the turning point of the curve due to the presence of a weaker rule of law.