

Impact Assessment of the Proposed Chemical Tax on Clothes and Footwear

The Fashion Industry – A Conscious Sector in Transformation

HUI Research commissioned by Svensk Handel (the Swedish Trade Federation)

September 2020

Summary

HUI has been commissioned by Svensk Handel to investigate the socio-economic consequences of the proposed chemical tax on clothes and footwear as proposed by Government Inquiry SOU 2020:20. In addition to calculating the financial effects, a number of interviews have been held with representatives of companies within the clothing and footwear industry.

The sector companies interviewed express a uniform view of the aims behind the legislation, namely to eliminate hazardous chemicals, as laudable and uncontroversial, but that when it comes expediency, the tax proposal has crucial shortcomings.

The tax takes aim at substances that the companies have already phased out in principle, and the extensive sustainability work that is being done in fashion companies risks being slowed, as internal resources will have to be switched from a proactive, risk based approach to what is perceived as unnecessary administration and unjustifiable testing activities. Calculations show that a third of the tax revenues that are expected to arise if the proposal comes into force are expected to come from products that do not contain any chemicals. The companies view the tax proposal as counter productive and instead suggest a series of alternative measures to hasten the phasing out of hazardous chemicals.

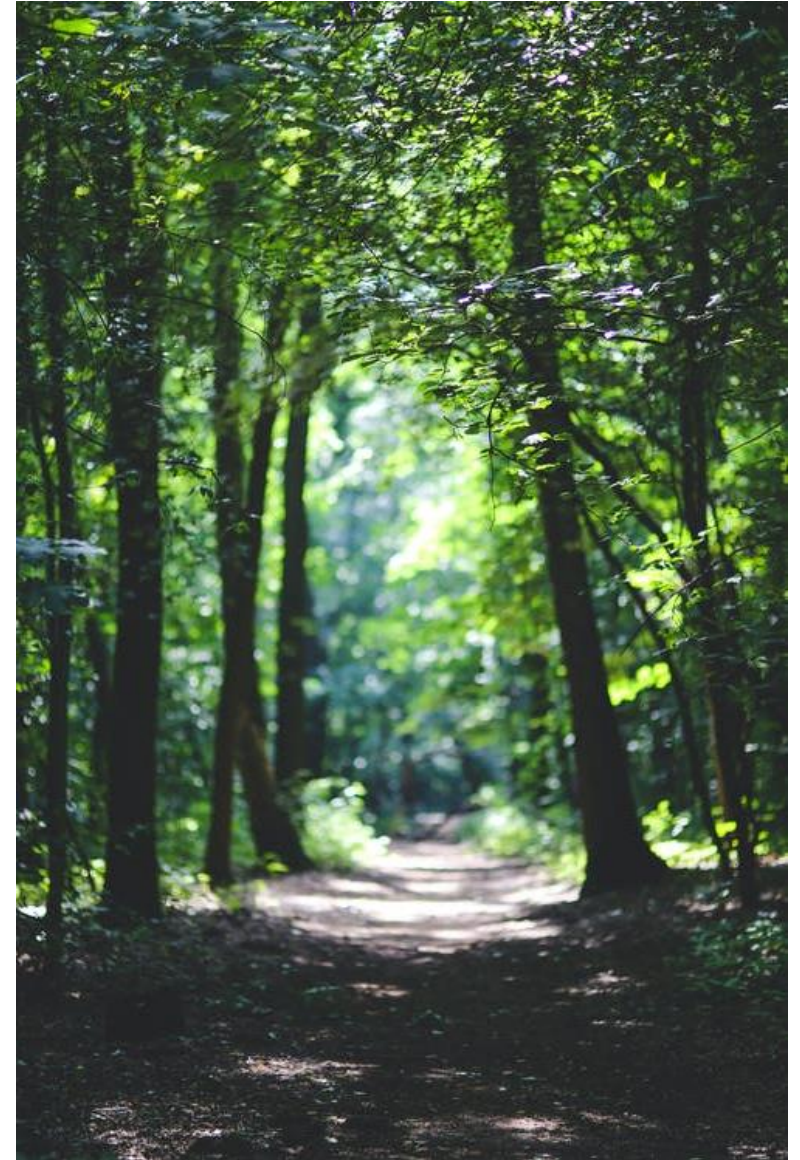
From a socio-economic perspective, one problem is that there is no way of knowing whether or not any possible benefits from introducing the tax would offset the significant costs that would arise for companies and consumers. As

such, there is a lack of socio-economic grounds for the tax.

The companies also face tremendous uncertainty in that the future application of the legislation by the Tax Agency will be of crucial importance for the financial consequences. What is clear, however, is that the tax can come to be far more cost driving than SOU 2020:20 expects it to be. The exact outcome will not least depend on what evidentiary requirements are applied to show that the products sold are free from the chemicals the legislators intend to regulate.

If the Swedish fashion trade, footwear trade and sporting goods trade respectively manage to pass on the increased costs to consumers, that are expected to add SEK 40 to the average pair of shoes than they would otherwise have cost, irrespective of whether or not they contain hazardous chemicals. When it comes to the effects on employment, 900 jobs are expected to disappear if the tax is introduced in the form currently proposed. Lessons learned from the chemical tax on electrical goods also show that there is a risk that the tax will be a zero sum game for government coffers and that jobs and big value will be lost without any discernible environment benefits.

Altogether, there are a many big question marks surrounding the expediency of the tax proposal, as it is clumsily designed and legally dubious. The importance of making effective, forward looking and risk-based sustainability work – an area where many Swedish fashion companies are leading the way – ought to be a high priority for decision-makers, companies and everyone else wanting to reduce the presence of hazardous chemicals.





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01 | The fashion industry today

A conscious sector in transformation

Fashion industry in transformation

The clothing industry and footwear industry, often jointly classed as the fashion industry, is in the midst of financial turbulence. The transition to online shopping, strong international competition, increasingly intensive sustainability work and the coronavirus pandemic are creating a challenging cocktail effect.

The fashion industry makes up a significant share of Swedish retailing. The sector accounts for 14 percent of total sales and around a quarter of durable goods retail stores. It is also important to bear in mind that a clear sector glide has made clothes and footwear important parts of the sports and leisure industry.*

In recent years, fashion retailers have become a shrinking presence on high streets and in shopping centres. From in many cases being the locomotive of retail areas, sales are increasingly switching to online. Both via traditional retailers opening online stores and fast-growing start-up online retailers. Added to which, international online stores have captured a big share of the Swedish market in a short space of time.

The fashion industry employs over 36,000 people around Sweden, of which almost 30 percent are in the 16-24 age group. Retailing in general and fashion retailing in particular, is an important springboard into the job market.

Consumption per head of clothes and shoes has not increased markedly over the past ten-year period. Between 2008 and 2018, household consumption of clothes and shoes increased by 11 percent in fixed prices.** The population increased by the same percentage, which means that per capita consumption stood still. According to household consumption expenditure (Statistics Sweden/SCB) on average SEK 720 a month was spent on clothes and shoes in 2019.

KEY FIGURES FOR THE SWEDISH CLOTHING AND FOOTWEAR INDUSTRY

57.5	4,512	5,480	0%	12%	20%	28%	65%
NET SALES, SEK BN (2018)	NO OF COMPANIES (2019)	NO OF STORES (2019)	GROWTH IN THE CLOTHING AND FOOTWEAR INDUSTRY (2019)	GROWTH IN E-TAILING (2019)	E-TAILING SHARE(2019)	NO OF EMPLOYEES 16-24 AGE GROUP (2018)	DEGREE OF CHAIN AFFILIATION (2019)

Source: E-Barometern (PostNord), SCB, Företagens ekonomi,RAMS, Butiksdatabasen, HUI/Handelsrådet



* the clothing and footwear share of total sales-of durable goods is probably a few percentage points higher when clothing and footwear sales in other sectors are included.

** Consumption Report 2019, Jan Magnus Roos (ed.), Centrum för konsumtionsvetenskap

The fashion industry – a victim of the pandemic

The Covid-19 pandemic has thrown everything on its head for the fashion industry, one of the retailing sectors hardest hit by far. Big sales losses have been the final nail in the coffin for many well-established companies.

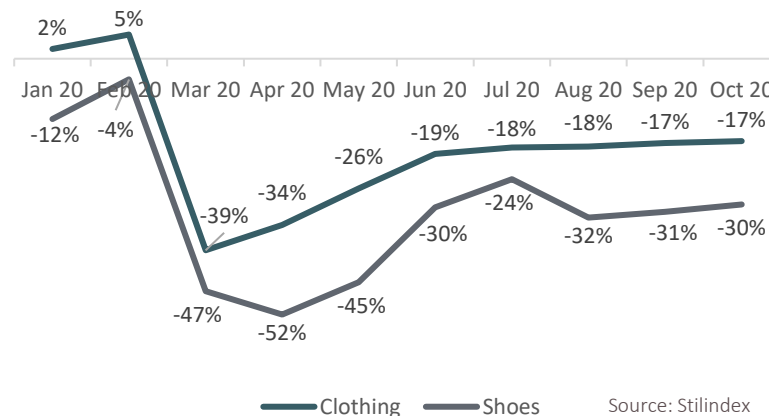
The spread of the coronavirus changed consumer behaviour and movement patterns overnight. Working from home and quarantining have resulted in lower visitor flows in stores and the associated lack of need for clothes and shoes for parties and everyday wear has led to fewer purchases. Data from Dagens Industri and Datscha for example, show that visitor numbers on retail high street Drottninggatan in Stockholm fell by over 80 percent in April 2020, compared to the same month the previous year.

The situation became unsustainable for many companies within the clothing and footwear industry that were already enduring poor economic growth, which has resulted in bankruptcy or reconstruction. Many smaller companies around the country have been forced to close their stores, as have a number of well-established and larger companies in the sector. Some companies that became bankrupt or entered reconstruction have since seen the light of day again with new owners or new capital, but the shake-out suggests that parts of the fashion industry lack sufficient reserves to manage sudden drops in revenues or increased costs.

Almost one in four employees in the clothing and footwear industry, over 14,000 employees, were put on short-term furlough until the end of June 2020.

While the durable goods sector as a whole has grown since the start of the pandemic, sales of clothes and shoes fell sharply during the months of restrictions. The footwear industry lost half its sales and the clothing industry a third of sales initially. The monthly slump has abated somewhat since then and shows a degree of stabilisation (see graph below), but the question is how many fashion companies will be able to survive losing a fifth of their sales in the somewhat longer term.

FASHION INDUSTRY GROWTH IN 2020



COMPANIES IN THE CLOTHING AND FOOTWEAR INDUSTRY THAT HAVE BEEN MADE BANKRUPT OR ENTERED RECONSTRUCTION IN 2020



Sustainability – a prioritised issue

Swedish consumers have shown a strong increase in commitment to sustainability issues over the past three years. Their biggest priority is that the products do not contain hazardous chemicals.

There is a big interest in the environment and sustainability in Sweden. According to the national SOM survey in 2018, interest in the environment scored 2.97 on a scale of 1 to 4 (CFK). The Svensk Handel Sustainability Survey in 2019 shows a similar result when six out of ten companies that have an active sustainability policy said that customer interest in sustainability had increased over the last year.

This interest is reflected in the fact that 93 percent of Swedish consumers state that it is important that the products they buy do not contain hazardous substances. Sustainability is also a factor that customers want stores to work more on, which generates a market-related competition rethink among companies.

From the companies' side, the connection between profitable and sustainable retailing is clearly established. 88 percent of companies within retailing say that there is a positive connection. Retailers also have the impression that customer interest in sustainability issues is growing year by year.

An increasingly popular and circular business model is second hand clothing. According to the Svensk Handel Sustainability Survey in 2019, three out of ten consumers had bought pre-owned everyday clothing in the past year, which makes clothing the most popular second hand products. An important part of the second hand market is the possibility of reworking recycled garments, that are resold in a new guise.

What's interesting is that regular second hand consumers tend to have a greater tendency to buy clothes in general. According to the 2018 national SOM survey, people who had bought second hand once or more times a month spend larger sums of money on clothes every month than people who did not buy second hand at all. The reasons for buying second hand seem therefore to be more than purely financial.

RETAILING COMPANIES FEEL THAT THEIR SUSTAINABILITY WORK
MAKES A POSITIVE CONTRIBUTION TO THE ECONOMY



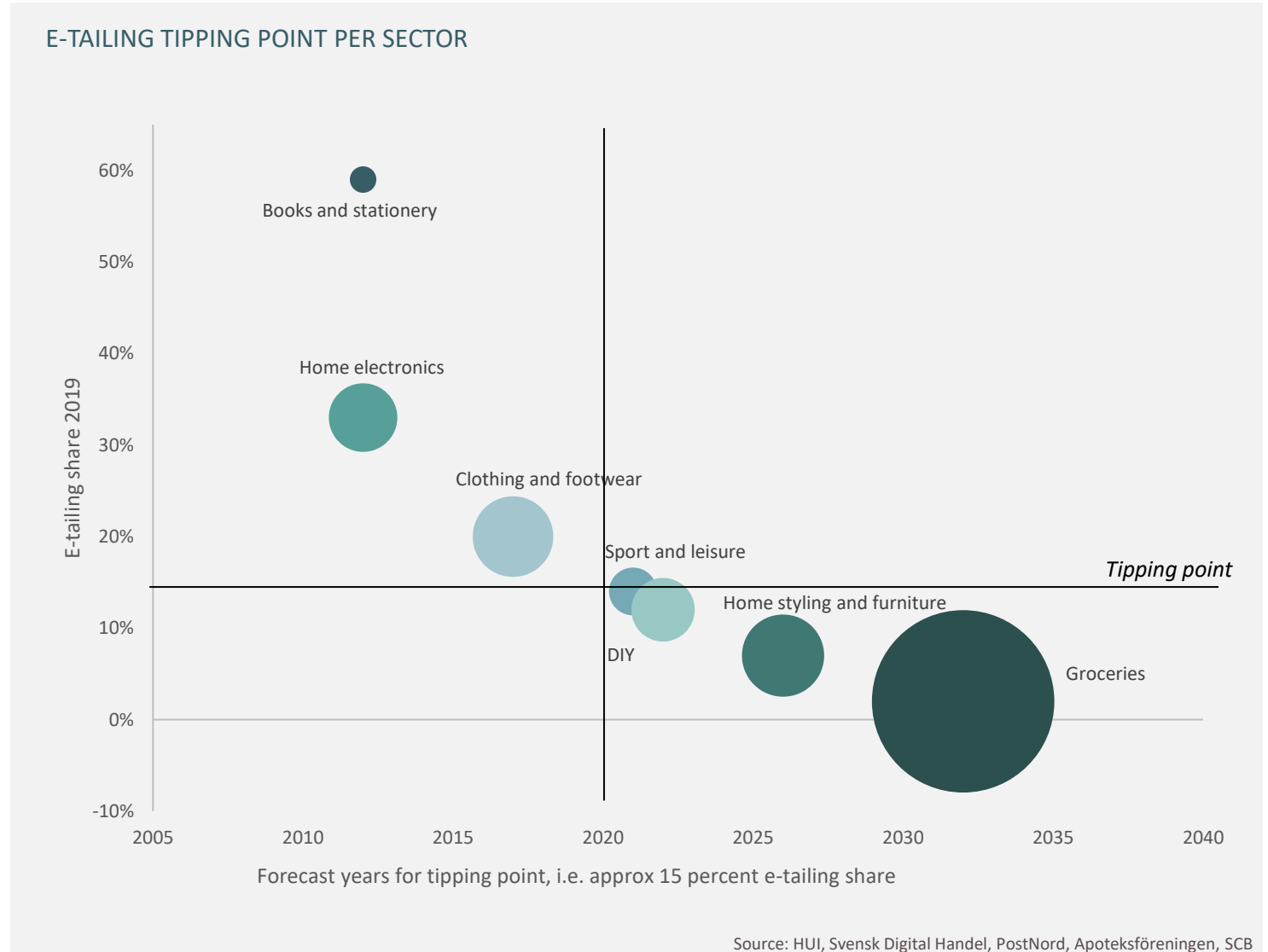
Passing the tipping point – growth is happening online

Almost all growth in clothing and footwear retailing is happening online.

In four of the past five years, clothing and footwear retailing has had e-tailing growth of over 10 percent. This has resulted in e-tailing having a 20 percent share of clothing and shoe retailing sales in 2019, a comparatively high figure.

When a sector reaches an e-tailing share above about 15 percent, all growth in the sector will very largely be found online. In recent years, fashion retailing has gone well beyond the tipping point where all growth moves online.

The sector was not first into digitalisation and nor has it come furthest. Home electronics and books and stationery have a higher e-tailing share and these sectors have seen several major consolidation and shake out waves. Next in line to reach the tipping point is sports and leisure retailing where clothing and footwear make up a big share of sales.



Digitalisation is squeezing profitability

When sales growth in physical stores stands still, business margins come under pressure.

Since surveys of sector growth online started in 2011, clothing and shoe e-tailing has grown by an average of 10 percent per year. At the same time, growth in bricks and mortar stores has been more restrained with a slightly negative growth over the same period. In 2019, 38 percent of online shoppers said that they had bought clothes and shoes online at some point in the last month, according to the PostNord e-barometer.

This increased digitalisation has reduced margins for parts of the sector. The average operating margin for companies in clothing and footwear retailing was 3.2 percent between 2014-2018. In the previous five-year period, the corresponding figure was 3.6 percent.

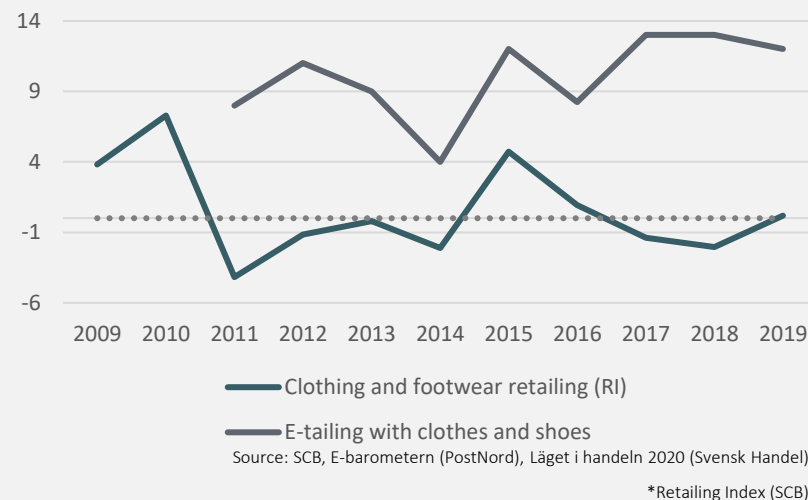
The biggest difference can be seen when the companies are broken down into quartiles. The lowest quartile had an operating margin of -4.4 percent in 2018 in clothes retailing and -4.5 percent in shoe retailing, compared to a median value of 1.7 and 1.3 percent respectively in these sectors. When it comes to net margin, that also factors in financial items, the figures are even lower for the lower quartile.

Over the last ten-year period, the lower quartile has constantly had a negative operating margin. The operating margin for the lower quartile of shoe companies has also fallen to the level after the financial crisis, even though there wasn't any such financial crisis during the period.

-4.4%

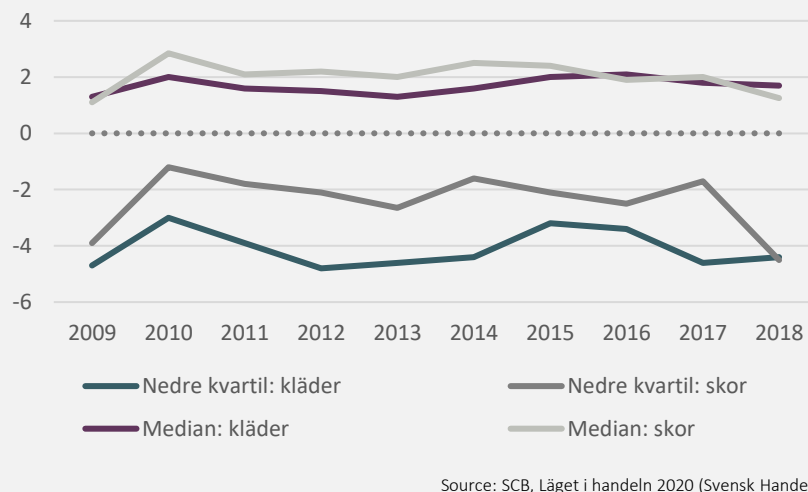
Operating margin
for the lower
quartile of clothing
companies in 2018

GROWTH IN CLOTHING AND FOOTWEAR RETAILING IN RI* AND IN E-TAILING
Annual change in percent, current prices



OPERATING MARGIN IN CLOTHING AND FOOTWEAR

Annual change in percent, current prices, lower quartile and median



The number of fashion stores is falling

The total number of stores in Sweden is falling. The biggest drop has been in the clothing and shoe sector. In 2019, there were around 5,500 stores in the sector, around 450 fewer than in 2017.

There tends to be fewer stores when more and more stores and companies consolidate. This reduction can be clearly seen in the city landscape, with temporarily empty premises and a smaller local range of clothes and shoe outlets. The visual difference is most clearly seen in smaller towns where each fashion store accounts for a larger proportion of the total range of clothes and shoes in the town.

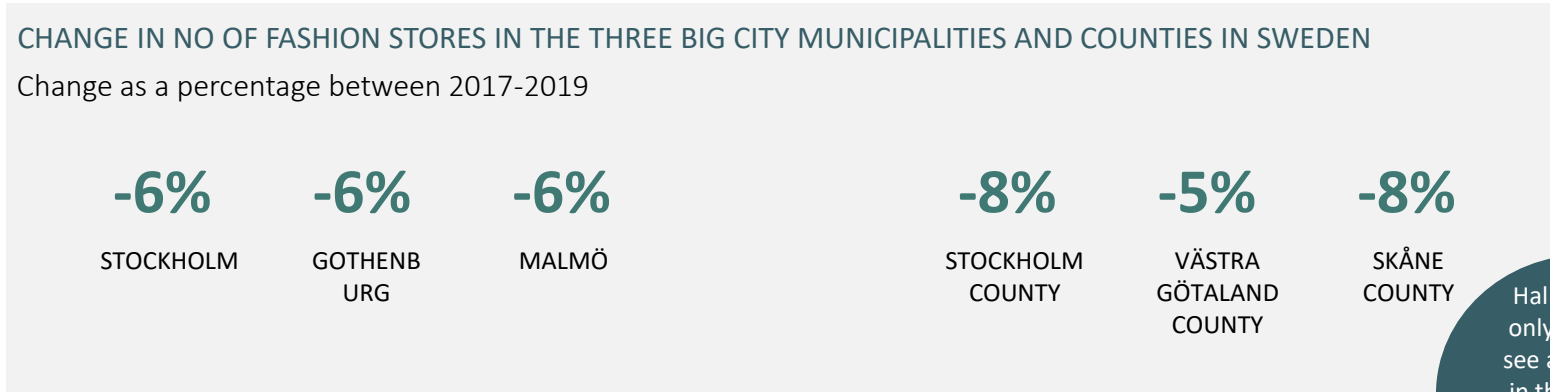
There have been regional differences in this development over the most recent two-year period. Halland on the west coast of Sweden is the only county where the number of fashion stores has increased

during the period, albeit marginally, while the biggest reduction has been in Västerbotten county in the north of Sweden. Just over one in eight fashion stores disappeared during the period.

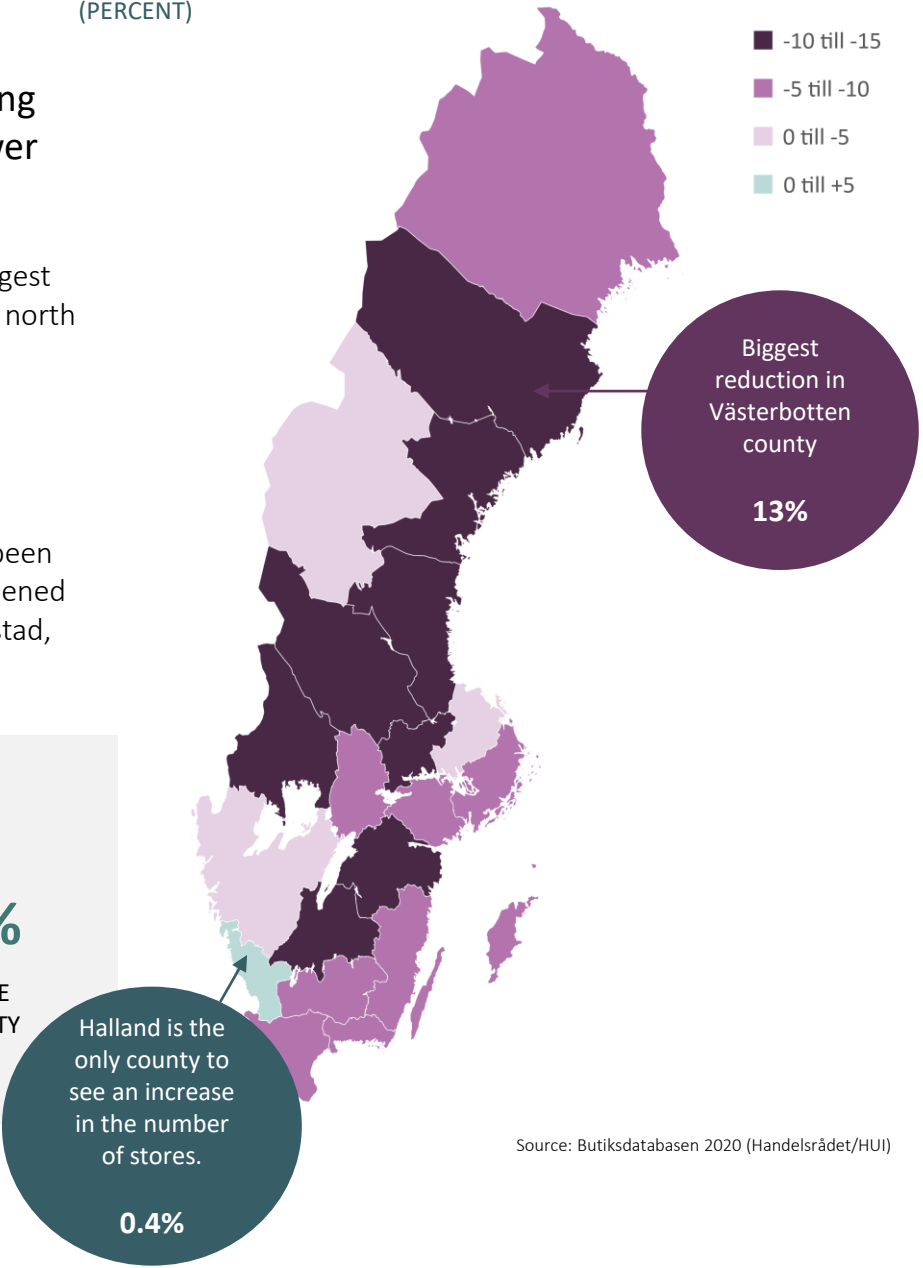
The number of stores in the three main cities of Stockholm, Gothenburg and Malmö has fallen by around 6 percent over the past two years. At municipality level, additional stores have mostly been in municipalities where shopping centres have opened during this period of time. These include Kristianstad, Mölndal and Kungälv.

CHANGE IN NO OF FASHION STORES IN THE THREE BIG CITY MUNICIPALITIES AND COUNTIES IN SWEDEN

Change as a percentage between 2017-2019



CHANGE IN THE NUMBER OF FASHION STORES 2017-2019 PER COUNTY (PERCENT)



Source: Butiksdatan 2020 (Handelsrådet/HUI)

Fashion is an international industry

Internationalisation is a double-edged sword for the fashion industry. If this happens on equal terms for Swedish and international retailers, both consumers and companies benefit, but tougher domestic requirements mean a competitive disadvantage.

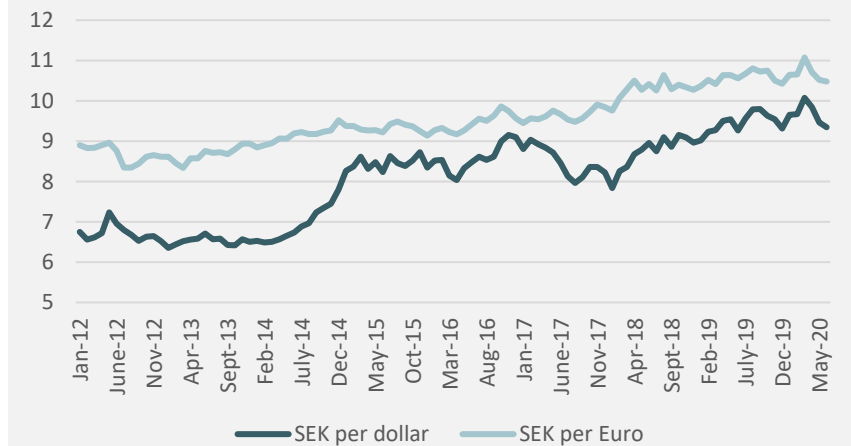
Goods retailing has become increasingly global over the past decade. Products from other continents are just a few mouse clicks away via e-tailing sites. For consumers, the internationalisation of retailing means a greater range and for retailers that launch their brands internationally, this opens up entirely new markets and revenue sources. However, for a local retailer with a physical concept, internationalisation, just like digitalisation, means greater competition for customers.

Clothes are the most popular product category among Swedes that buy online from abroad. According to the latest annual report from E-barometern, almost one in three consumers that have bought from abroad over the past month had bought clothes. International websites such as Zalando have grown rapidly on the Swedish market in recent years. Germany is the country most Swedes shop online from today, closely followed by Great Britain.

As a high proportion of fashion products sold in Sweden are imported, the SEK exchange rate plays an important role. The Swedish krona has been weak in recent years, which has meant higher purchase prices for importers. These additional costs have in turn not always been able to be passed on to consumers due to the greater international competition. As a result of these three parameters of digitalisation, internationalisation and a weak krona exchange rate has pressurised margins for traditional fashion retailers.

Corporate sustainability work is also done in an international context. Retail companies in Sweden have worked for a long time to make their products safe and free from hazardous substances. According to the Svensk Handel Sustainability Survey, retailers want to see tough requirements in order to move environment work forwards, but are of the opinion that tougher requirements in Sweden than in other parts of the world would put Swedish companies at a competitive disadvantage.

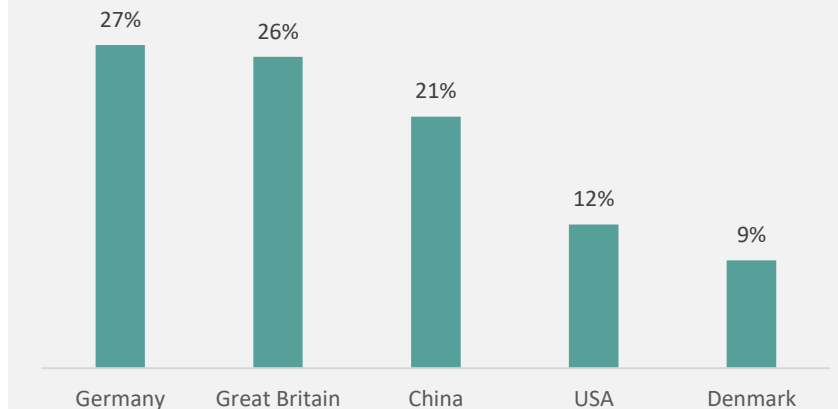
SEK EXCHANGE RATE AGAINST EURO AND US DOLLAR
2012- 2020



Source: Sveriges Riksbank, Ekonomifakta

THE FIVE MOST POPULAR COUNTRIES OUTSIDE SWEDEN

Base: Consumers that have bought online internationally over the past month



Source: E-Barometern (PostNord) 2019

02 | Fashion companies and the use of chemicals

On the international front line

Engaged chemical work – a Swedish tradition

Clothes and shoes are worn very close to the body. There is therefore a risk that chemicals in garments will be absorbed by the body. As one part of a long-running debate about research-based tougher restrictions concerning potentially hazardous chemicals, many Swedish companies in the clothing and footwear industry are pursuing ambitious efforts to nip use of these chemicals in the bud.

To bring greater clarity to the consequences of a possible tax on chemicals in textiles, HUI Research has interviewed representatives of companies in the sector who are well versed on the chemicals issue. The interviews show a great engagement in the issue and advanced work has been pursued within the companies to create a safe and secure environment for people that work in production and to ensure that no potentially harmful substances reach end customers. They all very largely offer the same reasoning for their hard work: “Obviously, I am just as keen as our customers in not wanting to have hazardous chemicals in my clothes.”



Quality in focus since 1936

Hestra has been manufacturing gloves of high quality for a long time. To take responsibility for the products, they own their production facilities and have worked on the chemicals issue for many years. “Striving for good quality will always be part of our DNA,” says CEO Anton Magnusson.

REPLACEABLE LINING FOR EXTRA SUSTAINABILITY

Hestra, a company in the south of Sweden, has a long tradition of producing gloves of the highest quality. Ever since the company was founded in 1936, quality has been an important aim, and the goal is to manufacture products that last for a very long time. To this end, Hestra gloves have replaceable linings, so worn parts can be replaced or repaired.

RESPONSIBILITY THROUGHOUT THE CHAIN

Hestra wants to be able to ensure that their products are ethically produced and that the products are of high quality. This has led to them owning their own production facilities, that are based in factories in China, Vietnam and Hungary.

In order to be able to lead proactive quality work, it is important to build long-term relationships with sub-suppliers. Hestra has worked with many of its suppliers for 20 to 30 years. This makes it easy to weed out unprofessional suppliers that do not live up to requirements.

CHROME FREE LEATHER SINCE 1986

It is important for Hestra to be a step ahead when it comes to sustainability work, and the company has been working to phase out hazardous chemicals for many years. One example is chrome free leather, that Hestra started introducing in their product range as far back as 1986. Today, Hestra does risk-based random testing of materials and products to ensure no hazardous chemicals are present.

THE TAX RISKS REDUCING SUSTAINABILITY WORK

Hestra gloves are of the highest quality and are made of many different materials. A drastic increase in testing and the significant administration that the tax risks entailing would have major consequences for a small business such as Hestra. Hestra follows the guidelines and thresholds set by the EU Reach regulation and in many cases, has stricter threshold limits on chemicals. Even so, the costs that the tax would entail risk reducing resources for other sustainability work, which would otherwise have benefited the company, consumers and the environment.



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Intelligent management ensures healthy shoes

Like many other fashion companies, Vagabond takes a proactive approach to eliminating hazardous chemicals. This approach permeates all areas of production, starting as early as the design stage. Vagabond also specifies tougher requirements than those in existing EU regulations.

PROACTIVE CHEMICALS APPROACH STARTS WITH DESIGN

Swedish footwear brand Vagabond puts a great deal of energy into ensuring its products are free from undesirable chemicals. Production is assured via strict controls all the way from prototype shoe to end consumers.

Vagabond aims to choose materials with the least possible negative health and environmental effects. The key is to work proactively by making all decisions on materials as early as at the design stage. The company's design studio, where sketches, prototypes, sole design and lasts take shape, is part of the head office in Varberg. Decisions on which material each component part should be made of and which supplier is to manufacture the footwear, are made at the same time. When a new shoe has been produced, the design package is sent to a local office in Vietnam that organises production.

EU REQUIREMENTS THE STARTING POINT – BUT VAGABOND GOES MUCH FURTHER

Vagabond is extremely careful about what chemicals can be found in its shoes. The company has its own chemical restrictions list based on the EU Reach regulation, but to which specific national legislation has been added. This means the company imposes tougher requirements than Reach – in terms of both what substances can be present and in what quantities. For example, chrome free tanned leather is used inside the shoes, the fabric lining is made of organic GOTS*-certified cotton and all polyester linings are made of GRS**-labelled recycled polyester. Natural plants are used to impregnate the leather.

Being in control of the entire process is also an important part of preparing for a more circular production process where materials are recycled to make new products. If such a process is to work, it is vital that no unwelcome chemicals are included in the materials from the start.

“We have now tested our first version of a sole made from recycled sole materials obtained from old shoes. A very small run, but it takes us another step closer to circular production.”

- Anna Fahle Björcke, Head of Communications at Vagabond

* Global Organic Textile Standard (GOTS) is an international label for clothing and textiles that includes both social and environment related requirements.

** Global Recycled Standard (GRS) is an international label where at least 50% of the material in an end product is recycled

The H&M Group aims to drive change

H&M has actively engaged in chemicals work since 1995, and has no intention of surrendering the leader jersey in this area. By continuously improving its chemicals work, the company aims to achieve full transparency by 2030.

H&M HAS THE DETERMINATION AND OPPORTUNITY TO CHANGE

“We aim to lead the change to safe products and a toxic free future for the fashion industry,” says Ylva Weissbach, sustainability expert within chemicals at the H&M Group. “We want to go from looking at what should not be used, to what alternatives are good. First we look at what function we want to obtain and then we will want to know what chemical is the best alternative in this context.”

CONTINUOUS CHEMICALS WORK SINCE 1995

Complex and global supplier chains test the patience of H&M personnel as the company strives to eliminate harmful chemicals from its textile production. The company introduced its first chemical restrictions in 1995 and over the past decade, the H&M Group has

been a driving force behind eliminating solvents in glue in shoes, phasing out perfluoroalkyl and polyfluoroalkyl substances (PFAS), and driving changes to find alternative chemicals in a number of areas.

H&M has sustainability / QA teams in all its production countries to continuously monitor compliance with its own restrictions list. Such control is also improved via a system called Input control, an IT tool that checks safety data sheets from chemicals manufacturers and ensures that the chemicals meet all the requirements specified.

“By 2030, we should have 100 percent recycled or other sustainable materials in our products and similarly, all products should be toxic free and we will know exactly which chemicals are used in production.”

The H&M Group has

25

years
of combined
experience of
chemicals work

The sector works together for a common chemicals agenda

The fashion industry is a global sector, and you need combined efforts to achieve change. Which is why the H&M Group works closely with many other industry leaders to make a difference.

With 4,900 stores on 71 markets and online sales on 47 markets worldwide, the H&M Group is one of a handful of textiles companies that have sufficient clout to influence clothes production on a large scale. To ensure the best results in a larger context, they often work closely with other companies.

For example, in 2011 the H&M Group initiated a partnership with Zero Discharge of Hazardous Chemicals (ZDHC), together with other fashion giants such as Inditex, Adidas, Levi's and Esprit, to eliminate discharges of hazardous chemicals. They also work with companies such as Nike, Ecco, Gap and Lacoste within the parameters of the AFIRM Group to develop common restrictions, better alternatives and testing methods. Together with AFIRM, the H&M Group has also created a common test matrix that charts how often different materials ought to be tested for each respective substance.



03 | Background to the proposed tax

A summary of SOU 2020:20

Tax of up to almost SEK 100/kg

In April 2020, the Inquiry that the government had appointed to consider the introduction of a chemical tax, presented its findings. The Inquiry put forward a proposal where seven groups of substances would be taxed by up to a total of SEK 78 per kg, excluding VAT.

THE TAX IS PART OF A SUBSTANTIVE POLICY PROGRAMME

In April 2020, the Government Public Inquiry (SOU 2020:20) that was commissioned to analysis and submit proposals on how a tax on hazardous chemicals in clothing and footwear could be structured, published its report. The background to the Inquiry was that a chemical tax on clothing and footwear is part of the substantive policy programme that the government parties have agreed on with Liberalerna and Centerpartiet. The tax is intended to reduce health problems for consumers that are exposed to the chemicals, to reduce environment problems arising during manufacture, washing and waste, and to increase the quality of recycled materials. The tax is proposed to come into force on 1 April 2021.

UP TO SEK 78 PER KG PLUS VAT

The Inquiry proposes a weight based tax, where the presence of seven groups of substances determines how much a product should be taxed. The tax ranges from SEK 2 to 78 per kg on products sold, and is divided into three levels. The taxed amount is liable for VAT, which results in a mark-up from SEK 2.5 to 97.5 per kg.

THE THREE TAX LEVELS

SEK 40 per kg

In principle, the tax covers all clothing and footwear and is levied on products that contain hormone interfering substances PBT/vPvB, allergens, CMR or biocides.

Products where either none or only one of these substances respectively is present, will be permitted tax relief of 95 and 47.5 percent respectively.

SEK +19 per kg

The tax covers products that consist, wholly or in part, of soft made polyvinyl chloride, polyurethane or rubber and is levied in cases where these contain phthalates.

SEK +19 per kg

The tax covers products that are designed for all weathers, and is levied in those cases where they contain perfluoroalkyl and polyfluoroalkyl substances (PFAS).



Burden of proof falls on the fashion companies

The proposed tax affects virtually all clothes and footwear. In those cases where the products are entitled to tax relief, it is the companies themselves that are responsible for submitting sufficient evidence to the tax authorities. Evidence is obtained with the help of manufacturer certificates and own lab tests.

COMPANIES AND PRIVATE INDIVIDUALS LIABLE FOR TAX

In principle, the tax covers all clothing and footwear, whether made from textiles, leather and synthetic leather, fur, fake fur, or rubber. Exactly which products will be liable for tax will be specified via the customs tariff KN reference number. According to the proposal, companies that have annual sales of over SEK 100,000 for these types of products to consumers in Sweden will be liable for the tax. The Inquiry assesses that just over 7,000 companies will be affected. In other cases, the distributor of the product, or the private individual who buys products from a company below this limit, will be liable for the tax.

COMPANIES ARE LIABLE TO PROVIDE EVIDENCE

Tax relief is allowed in cases where the products do not contain more chemicals than that specified in the tax threshold. The party liable for the tax is liable for submitting sufficient evidence to the tax authority to qualify for relief.

Exactly what evidence is required is not made clear in the proposal, however. The tax authority will determine whether the evidence is sufficient from case to case. The Inquiry assumes that declarations of content and certificates from the product manufacturer will often be adequate proof, but not always. Companies can support their production of evidence by performing extensive own checking of the content in their clothes and shoes, and the Inquiry assesses that such own checks will increase as a consequence of the tax. Measuring the content of chemicals should be done on all homogeneous materials in the product.



One in six garments contains hazardous substances today

The Inquiry assesses that 16 percent of all clothing sold in Sweden contains one or more hazardous substances, while 84 percent do not contain any of them.

ONE PERCENT OF CLOTHES CONTAIN TWO SUBSTANCES

There is relatively little knowledge about how common the substances concerned are. The Inquiry has therefore relied on older research, and has estimated how the incidence of these substances has changed, in order to assess how big a presence each respective substance has today. A random sample study was also performed for footwear, to chart such presence. The estimated incidences are presented in the table right.

The Inquiry estimates that the probability of a garment containing three or more substances is one in 2,500. 1.1 percent of the clothes are expected to contain two substance groups, 15.2 percent are expected to contain one substance group and 83.7 percent of the clothes are expected to not contain any of the substances.

The Inquiry also assumes higher proportions in clothes that are directly imported rather than those that are sold from Sweden and the EU. The proportion of clothes directly imported from countries outside the EU is expected to be 5 percent, but this is expected to fall to 4.8 percent if the tax is introduced.

MASS FRACTIONS ASSUMED

Estimated presence of respective substance group in clothing and footwear, 2019

	Clothing	Footwear
Phthalates	1.2%	2.0%
PFAS	2.6%	16.6%
Hormone interfering substances	8%	12.6%
Biocides	1.9%	1.0%
PBT/vPvB	5.1%	3.5%
Allergens	2.0%	0.5%
CMR	0.5%	0.5%

04 | Socio-economic analysis of the tax proposal

Consequences from a societal perspective

Reasoning behind the chemical tax

The underlying argument for taxing clothing and footwear rests on a phenomenon that within economics is described as external effects. What does this mean and what are the grounds for a practical policy?

EXTERNAL EFFECTS

The argument for introducing a tax that targets hazardous chemicals concerns so-called *external effects* or *externalities*. An external effect (or externality) within economics is a consequence of a given transaction where the affected party does not form part of the same transaction. If the effect is negative it is called an *external cost*, i.e. a cost that production of the product that is sold gives rise to but which is not reflected in the price. The phenomenon is illustrated to the right, where A sells a product to B, which entails an external cost to C.

CHEMICALS AS NEGATIVE EXTERNALITIES

The SOU 2020:20 Inquiry considers that certain chemicals that arise in clothing and footwear entail significant external environmental and health costs for the public that the fashion industry and consumers respectively avert their eyes from in their exchange. What is named as giving rise to these costs is bodily exposure to hazardous substances, pollution of wastewater when washing clothes and emissions from discharges during production.

CORRECTION OF EXTERNALITIES

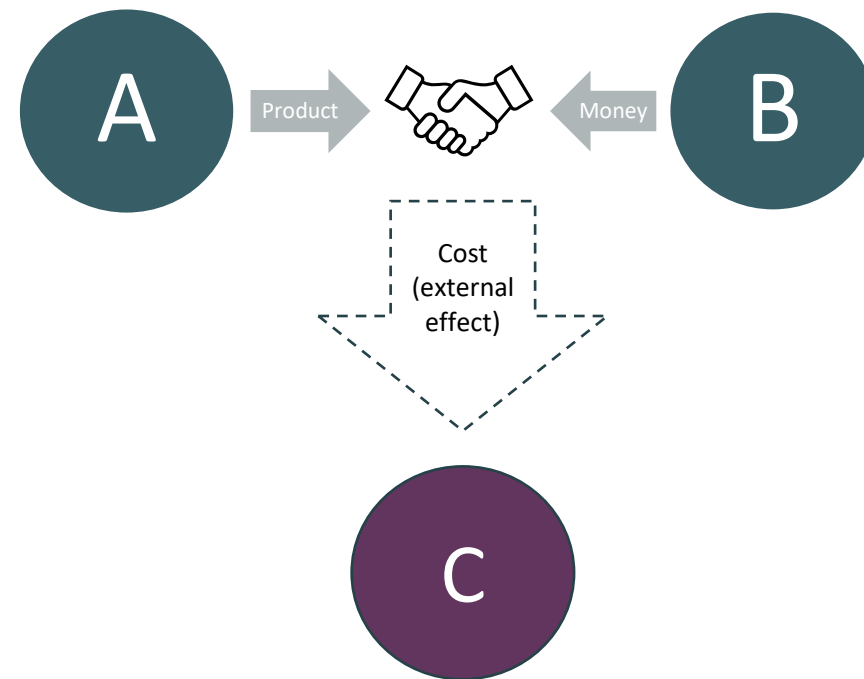
Taxation is an alternative to correct externalities that is a big topic for discussion within economics theory. Without taxation, the production cost is said to only consist of the so-called *private* production costs (e.g. costs for input goods and wages) but not the external cost, which gives rise to overproduction. If the government raises the production cost via an excise duty that corresponds to the external cost, a more optimal outcome is considered to be achievable.

CORRECTIVE CONDITIONS

An efficient correction of a negative externality via taxation is based on two things:

1. The size of the externality is known or can be estimated with reasonable reliability.
2. The cost for correction is less than the external effect.

As we will see on the next few slides, the first condition is not satisfied in the case of the proposed tax. A view cannot therefore be taken on the second condition, but the costs for action would be extensive.



The external effect is unknown

To achieve effective taxation correction, the external cost must be known or able to be estimated with reasonable reliability. This is not the case with the proposed chemical tax on clothing and footwear.

INFORMATION PROBLEM FOR TAXATION

Quantifying external effects is very difficult, as it concerns costs that by definition have not been priced. This lack of information is a fundamental problem. It can be argued that the government has greater scope to gain an understanding of the technical consequences of different chemicals than consumers, but this is not enough. Even if all relevant causal connections could be established, there has been a lively debate within economics as to whether or not identifying the correct cost is possible. The cost is made up of subjective valuations of consequences that are never determined for legislators or anyone else. Arthur Pigou, who first came up with the idea of duty as a way to correct negative externalities, wrote for example:

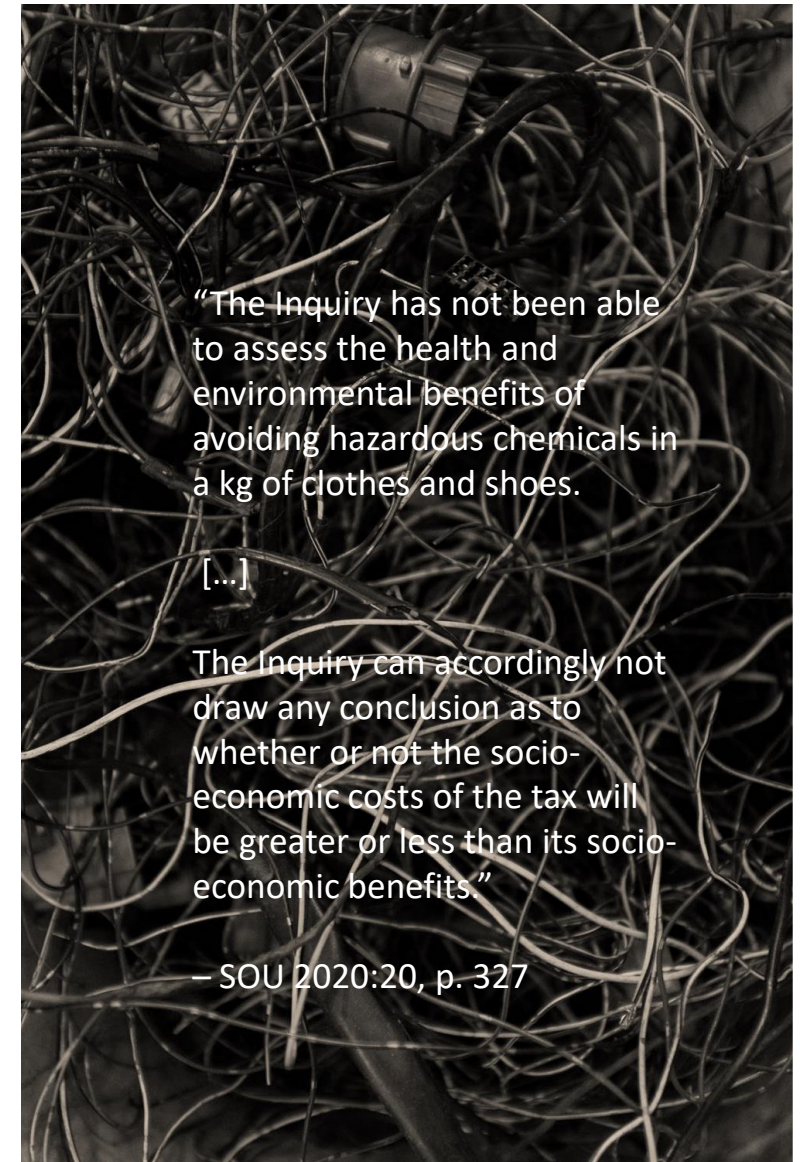
“It must be confessed, however, that we seldom know enough to decide in what fields and to what extent the State, on account of them, could usefully interfere with individual freedom of choice. [...] ‘Fancy’ finance, like a fancy franchise, whatever its theoretical attractions, has, at all events in a democracy, dim practical prospects.”*

IGNORANCE OF THE EXTERNAL EFFECT IN THE CASE OF CLOTHING AND FOOTWEAR – SPECIFIC PROBLEMS

Information or the lack of it, is clearly a problem in the case of the proposed tax on clothing and footwear. In the first instance, there is a lack of information on the chemical content in the products that are intended to be taxed, other than that the analysis of the presence of the chemicals as such, and is based on a long list of uncertain assumptions. Secondly, there is a lack of knowledge on the causal connections between different content levels of the chemicals in question and possible costs for the environment and health, in accordance with people’s valuation.

SOU 2020:20, that forms the basis for the proposed chemical tax on clothing and footwear, clearly accepts this reservation:

“The Inquiry has not been able to assess the health and environmental benefits of avoiding hazardous chemicals in a kg of clothes and shoes. [...] The Inquiry can accordingly not draw any conclusions as to whether or not the socio-economic costs of the tax will be greater or less than its socio-economic benefits.” (p. 327)



“The Inquiry has not been able to assess the health and environmental benefits of avoiding hazardous chemicals in a kg of clothes and shoes.

[...]

The Inquiry can accordingly not draw any conclusion as to whether or not the socio-economic costs of the tax will be greater or less than its socio-economic benefits”

– SOU 2020:20, p. 327

*Arthur C. Pigou, *Some Aspects of the Welfare State*, p. 6

The cost for “correction” is extensive

One problem with the attempt to manage the possible health and environmental effects of clothing and footwear with the aid of taxation is the intervention that in itself, gives rise to costs. These costs – partly external – can be greater than the effects intended to remedy.

INTERVENTION CREATES ITS OWN EXTERNALITIES

Corrections of external effects are possible in a world where the size of externalities is known, but even in such cases, intervention by legislators is not a self-evident alternative. The intervention occasions new costs that must be taken into account. To the extent it is citizens that are assumed will suffer health problems and possible injuries from chemical-based production, the purpose of an environment tax must be to compensate the collective citizenship for such suffering. Optimal allocation therefore requires revenues from the tax to go back to citizens, e.g. via tax switching. This means that the administration authority and inspection necessary to achieve the aims of the interventions cannot be self-financing from the new tax revenues to be justified in terms of welfare economics. The tax can certainly be set at a higher rate than that justified by the external cost of the chemicals, but you would then create an underproduction of clothes and shoes.

The following are key to the costs of the tax:

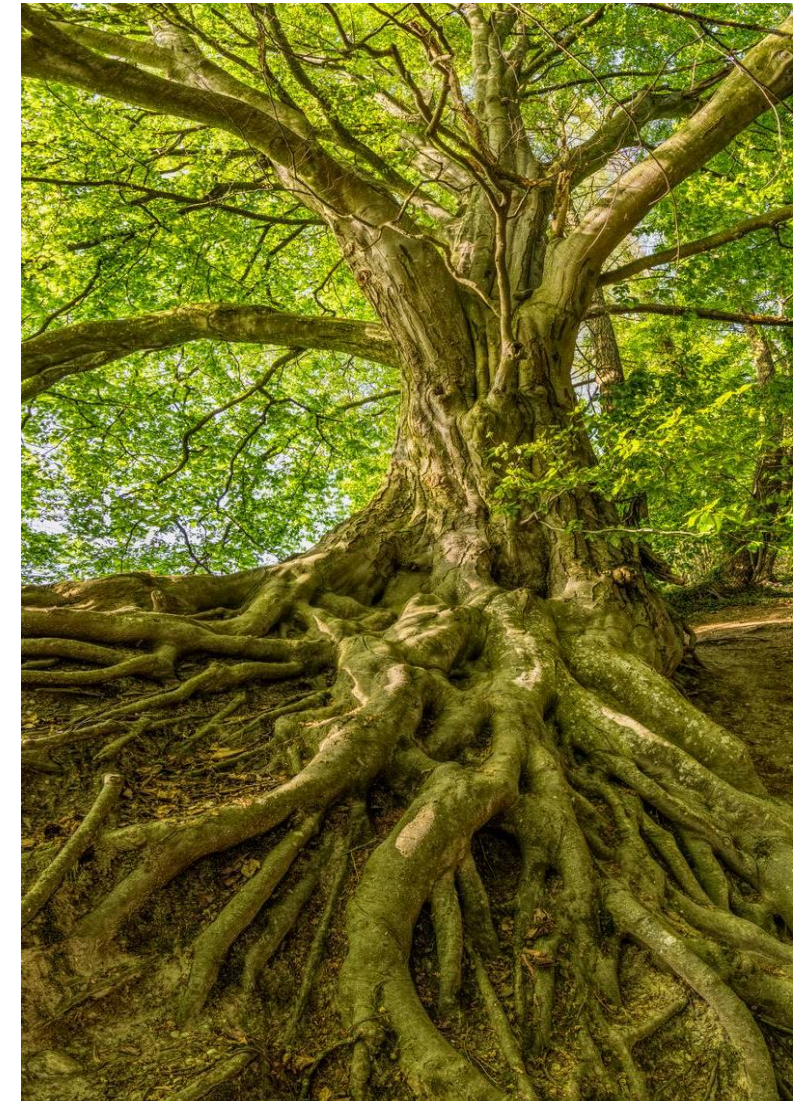
- *Companies' costs.* Costs arising for checks on the chemical content of products, running tax administration and increased purchase prices as a result of the requirements specified on suppliers. This not only means labour costs but also in certain cases, the companies can need to make substantial investments in e.g. IT support to deal with administration.
- *Public authority costs* for greater inspection, monitoring and administration duties.
- *Reduced consumer surplus.* In addition to fewer purchases and poorer functionality in cases where there is a lack of substitutes for the chemicals, the effect will be less consumer choice in the Swedish fashion industry. Small scale purchases and special orders of products become unprofitable. In the case of products that consist of many different materials (e.g. footwear), this effect is expected to be even more apparent.
- *Demoralisation of entrepreneurs and companies,* which reduces the rate of investment, leading to fewer jobs and increases entry barriers to the fashion industry.



Consequence assessment: assumptions

A large number of assumptions have to be made to calculate the consequences of the proposed tax. Here, we present the assumptions made by HUI and how these relate to the calculation assumptions made in the consequence analysis of SOU 2020:20.

- **The tax burden and increased administration will be passed on in full to consumers.** This assumption is also made in SOU 2020:20. The price increase caused by the tax itself, administration costs for companies and VAT on top of the tax.
- **The incidence of chemicals.** The same assumptions are made about the presence as in the SOU, for example, that the relevant chemicals will not be found in 84 percent of all clothing. See also slide 21.
- **No of products that require documentation.** HUI has, based on searches on price comparison sites and in large retailer online stores, estimated that there are around one million products within clothing and footwear in Swedish retailing, and that each product is available at two different vendors on average.
- **Companies' administration.** Each product is assumed to require at least one extra hour of administration at a unit costs of SEK 300. Lab testing is assumed to correspond to 1 percent of all verifications. The latter assumption is very uncertain but is based on the Inquiry formulations, interviews with sector companies and talks with the Swedish Tax Agency about their experience of the chemical tax on electronics.
- **Market definitions.** Sales in the calculation are based on the SNI code statistics in accordance with the SCB database *Företagens ekonomi*. Clothes retailing is defined as SNI 47.71 and 47.912. Footwear retailing is defined as SNI 47.72. Sports retailing is defined as SNI 47.64 and clothing and footwear are assumed to account for 75 percent of sales in the sporting goods sector.
- **Price per unit of weight.** For clothing, the data are based on import statistics from SCB, which works out at just over SEK 600 per kilo. SEK 800 per kilo has been used for shoes, based on checks with shoe companies and random tests in online stores.
- **Own price elasticity on clothing and shoes.** HUI assumes -0.65 for both clothes and shoes. SOU assumes -0.8 for clothes and -0.4 for shoes.* The SOU accordingly uses a separate elasticity for clothes and shoes. HUI's assumptions are based on the average of two studies with specific data for Sweden, while the SOU is based on an international study.
- **Turnover efficiency.** HUI estimates that as a consequence of the Covid-19 crisis, turnover per employee within clothing and footwear retailing will have fallen by 10 percent between 2019 and when the tax is introduced in 2021.



*HUI has used the short term elasticity found in Assarsson, 2004, *Consumer demand and labor Supply in Sweden 1980-2003* plus the elasticity in Kemper, 2018 *Cross-Cultural Differences in Online Elasticity*.

Legal uncertainty and high test costs

The tax edifice rests on a lack of legal certainty. The Swedish Tax Agency application puts the burden of proof on companies, but future interpretations of the law by the authority on the issue are unknown and at the same time absolutely crucial to the financial consequences of the tax.

TREMENDOUS LEGAL UNCERTAINTY

One big problem that the companies are experiencing with the proposal is the tremendous legal uncertainty surrounding how they are expected to verify the chemical content of their products. According to SOU 2020:20 (p. 291), the Swedish Tax Agency is to resolve “from case to case” what documentation is required, which means that the companies must guess how the Tax Agency will apply the evidentiary requirements. This is a fundamental uncertainty as the financial consequences of testing differ substantially from the financial consequences of alternative methods to proving that products do not contain chemicals, such as product declarations or certificates from suppliers.

POSSIBLE UNDERESTIMATE OF TESTING COSTS

Given that certificates from suppliers is a far cheaper method than testing to support deductions, HUI assumes that companies – unless other directives are issued – will test products to the extent that (1) other verification methods are not possible, (2) to ascertain that suppliers are issuing correct certificates, and (3) in cases where the Tax Agency performs an audit and asks for supporting data other than laboratory certificates.

The first two points above are likely to be the most significant. In its calculations, HUI has assumed a test frequency of 1 percent. The SOU assumes that the tax will lead to 30,000 extra lab analyses at a cost of SEK 2,000 per analysis. However, the SOU also states that package analyses including various sub tests often cost from SEK 5,000 to 16,500 (p. 140). HUI assumes an average cost of SEK 2,000 per *substance test and material*, as this is in line with what has emerged in HUI interviews with companies in the sector. A further assumption is that two materials will be tested for clothing and five for shoes. The cost per analysed material will be higher than that stated in the SOU when you factor in the need to check several materials for the different substance groups that the tax is aimed at when testing is actually done. The additional costs for lab analyses (of over 40,000 materials or 15,000 garments), would then be around MSEK 470, rather than the MSEK 60 the Inquiry estimates. More administration and adaptation costs must also be added to these test costs.

SMALL BATCHES WILL BE UNPROFITABLE

The maximum tax relief for the bulk of all products would be SEK 38 per kg. This means that orders of less than around 300 kg of clothing or footwear would be unprofitable for companies where lab tests are required.



900 lost jobs

The introduction of a chemical tax would mean higher prices on clothing and footwear and a fall in sales. This would affect employment, the number of companies and tax revenues.

JOBS AND COMPANIES WOULD DISAPPEAR

HUI’s calculations show that 900 jobs risk disappearing if the tax were introduced in the proposed form. The shake-out effect amounts to around 150 companies within the retail sector.

HIGHER PRICES FOR SWEDISH CONSUMERS

The consequence analysis in SOU 2020:20 estimates that prices will rise by 4 percent on those products not eligible for tax relief. HUI’s calculations suggest average price increases of 2 percent on clothing if the effect were to be across the board on all garments. However, the price effect on footwear is assessed as being significantly higher and corresponds to an increase of 7 percent. The average pair of shoes, whether or not they contain the relevant chemicals, can therefore become over SEK 40 more expensive than today. According to HUI’s calculations, the average Swedish household would face an annual increase of SEK 230 for clothing and footwear purchases, even though the household is expected to consume a somewhat smaller quantity of clothing and footwear than would otherwise be the case.

FOOTWEAR RETAILING ESPECIALLY VULNERABLE

The tax would mainly hit clothes retailers, footwear retailers and sporting goods retailing. In relation to the size of this sector, HUI expects the greatest effects on footwear retailing because shoes contain many different materials and probably have a higher content of those chemicals the tax is aimed at, than clothing. According to our calculations, the loss of sales in footwear would amount to 4.6 percent, while the drop in clothes sales is estimated at 1.3 percent and sporting goods 1.2 percent. If the tax is introduced in 2021, this would put a real brake on the recovery that is expected after the dramatic downturn we have seen in 2020.

RELATIVELY MINOR EFFECT ON PUBLIC FINANCES

A reduction in consumption means the loss of VAT revenues and the loss of jobs also means less tax and other charges on salaries. The estimated effect on public finances of MSEK 340 corresponds to around 0.3 per mille of the government budget. The plus effect for the government will clearly be less than the minus effect for companies, as in addition to paying the chemical tax itself and extra VAT, companies will also need to cover the costs of lab tests and increased administration.

Analysis comparison	HUI Research	SOU 2020:20
Price raising effect	<ul style="list-style-type: none">+2% on average on all clothes+7% on average on all footwear	+4% on those products that contain chemicals
Effect on net sales	-1.6% of which effect on Clothes retailing: -1.3% Shoe retailing: -4.6% Sporting goods retailing: -1.2%	-1.1%
Effect on no of employees	-900 jobs	-700 jobs
Effect on no of companies	-150	< 100
Tax revenue (chemical tax gross)	MSEK 690	MSEK 790
Effect on government finances	MSEK 340	MSEK 750

Alternative corrective methods

In addition to the taxation alternative, two solutions to the problem of external effects are addressed extensively in the research literature. Both bans and self-regulation have played a key role when it comes to phasing out chemicals within clothing and footwear retailing in recent years.

TAXES, BANS OR SELF-REGULATION?

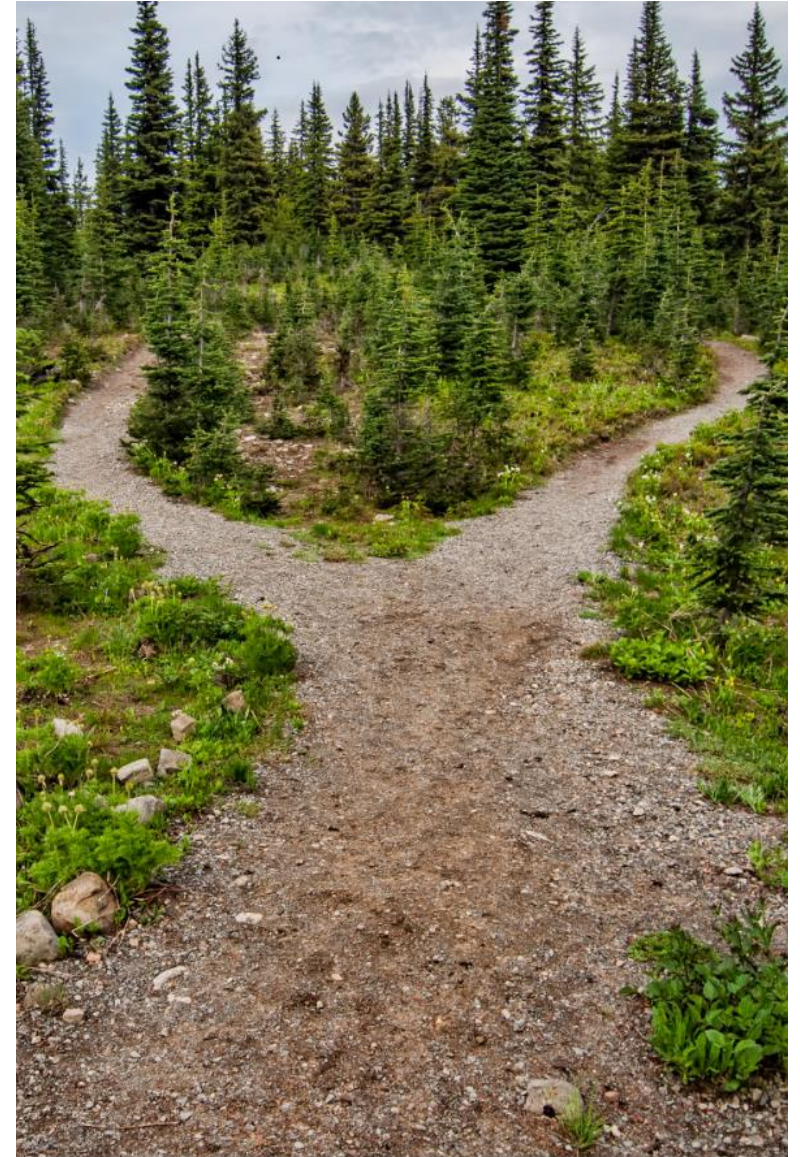
In addition to taxation, two alternatives are extensively looked at in the literature as a solution to the problem of external costs:

- **Bans.** This method has been viewed by many economists as only relevant when there are other goals than purely socio-economic ones that motivate very far-reaching interventions. One problem with bans can be that all the benefits the banned product after all offers would disappear. Sometimes, there can be no substitutes for the regulated product, which means that a ban will have a very high cost in terms of lost customer benefits.
- **Self-regulation.** This is based on the third party facing the external cost having the incentive to take action to address the causes. If information emerges that chemicals risk the health of citizens, certain incentives arise for citizens as a collective to turn to consumer and environment organisations for example, to pressurise companies to reconfigure their production. Consumer pressure on companies to actively eliminate hazardous substances that are frequently used in products and worn close to the

body has increased in recent years. Negative media publicity concerning the use of unjustifiable chemicals and the risk of a boycott can be significant incentives for companies to react, if the damage from such negative publicity can be expected to be greater than e.g. the practical benefits that arise as a consequence of using these chemicals.

RAPID PHASE OUT OVER THE PAST TEN YEARS

The SOU Inquiry also explains in its consequence analysis that many of the chemical groups for which greater regulation is intended, have more or less been phased out over the past ten years, primarily due to increased pressure, extensive self-regulation among companies and the EU Reach regulation. This phasing out has been dramatic in many cases, which indicates that self-regulation with elements of prohibition have been a successful combination. To name one comparison, phthalates, a substance group that the SOU Inquiry assumes to have been present in 0.5 percent of all T-shirts in 2019, was found in 7 percent of T-shirts 10 years before (SOU 2020:20, p. 277).



Fiscal and political profit maximisation

One explanation as to why taxation is often a popular option in practice, is that it concerns incentives when structuring a new policy.

THE PUBLIC CHOICE SCHOOL AND PUBLIC SECTOR BODIES

It has long been known within economics that public sector bodies, as in the private sector, are characterised by incentives to preserve their own self-interests and to maximise gains in a broad sense. For example, politicians are interested in votes and public authority executives in the allocation of resources and powers of governance. This insight forms the basis for the so-called public choice school within economics, where James Buchanan and Gordon Tullock are prominent representatives. The former was awarded the Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel for his work.

POWERFUL INCENTIVES FOR THE TAXATION OPTION

It is worth noting that different policy measures are not equivalent from an incentives perspective. While a *ban* entails a reduction in government resources as a consequence of the costs that arise to uphold new legislation, as a rule, the *taxation option* means the governing power's resources increase (at the expense of private sector body resources). In the case of *self-regulation*, the government finance effect is zero.

An optimal measure from the political self-interest perspective, is therefore not seldom a tax that generates as much revenue as possible but that at the same time does not place a heavy work load on politicians. In the event this type of incentive dominates, the result is overtaxation and distortions, as what is socio-economically optimal does not necessarily coincide with the self-interest of political bodies.

HOW THE CHEMICAL TAX IS STRUCTURED

The public choice perspective can also contribute to explaining why certain tax structures become particularly popular. In particular, this concerns structures where the tax base is made as broad as possible. In the case of the chemical tax on clothing and footwear, the Inquiry has chosen to propose a basic charge on all clothing and footwear independent of the chemical content, where the burden of proof for possible relief resides with the companies. According to HUI's calculations, one third of the tax revenues is expected to come from products that are entirely free of the chemicals regulation is aiming at. This, as SEK 2.5 per kg (incl. VAT) is proposed to be charged on the broad tax base that does not contain chemicals – 84 percent of all clothing according to the SOU estimate.

Fiscal consequences of different regulatory measures

Schematic overview

	Taxation	Ban	Self-regulation
Revenues for government?	Yes	No	No
Costs to government?	Yes	Yes	No

Proportion of tax from garments that are free from chemicals

Calculation assumptions according to SOU 2020:20

0 substances	1 substance	2 substances
Ca 84% of all garments	Ca 15% of all garments	Ca 1% of all garments
Tax: SEK 2.5/kg incl. VAT	Tax: SEK 26.25/kg incl. VAT	Tax: fr SEK 50/kg incl. VAT
$\frac{(84\% \cdot 2,5)}{(84\% \cdot 2,5 + 15\% \cdot 26,25 + 1\% \cdot 50)} \approx 1/3$		

05 | Burden of proof rests on fashion companies

Consequences and improvement proposals
from the retailer perspective

The burden of proof residing with fashion companies – Consequences

THE INDUSTRY VIEW – INTERVIEWS WITH FIVE COMPANIES

A tax on hazardous chemicals in clothing and footwear will have a big impact on fashion company costs, sustainability work and administrative processes as the burden of proof resides with fashion companies.

To gain a clearer picture of the consequences of the tax for the companies, HUI has held in-depth interviews with five companies on the market:

- Lindex (clothing)
- Hestra (gloves)
- Stadium (sporting goods)
- Kavat (footwear)
- H&M (clothing)

This section is a summary of the views and conclusions that emerged during the interviews.



The industry views the intentions behind the tax as positive

The clothing and footwear sector has long been addressing the chemicals issue, and all the companies interviewed have working actively to address and phase out those chemicals that the tax concerns in their own production for many years. The industry therefore views the intentions behind the tax of reducing the presence of hazardous chemicals as positive. But – the hazardous chemicals the Inquiry lists have very largely been eliminated long ago.

POSITIVE REACTION TO TAX INTENTION

All the companies interviewed are positive to the government imposing tougher demands on chemicals usage. The elimination of harmful and environmentally hazardous chemicals is seen as an important issue within the industry and many companies take a proactive approach. The companies also perceive an increased awareness of and greater interest in these issues among customers, especially when it comes to products for children. All the companies interviewed therefore phased out these chemicals from their own production many years ago.

ENGAGED CHEMICAL WORK

All the companies interviewed have been working for a long time to eliminate chemicals suspected of being potentially harmful for the environment or consumers. One example is Lindex, that performs chemical tests on its products and can clearly see that their work has reduced the presence of undesirable chemicals. In 2019, Lindex performed 658 production tests, of which undesirable chemicals were found in nine cases, which corresponds to 0.6 percent of the products tested. It is important in this context that such tests are done before shipping and no rejected products reach consumers.

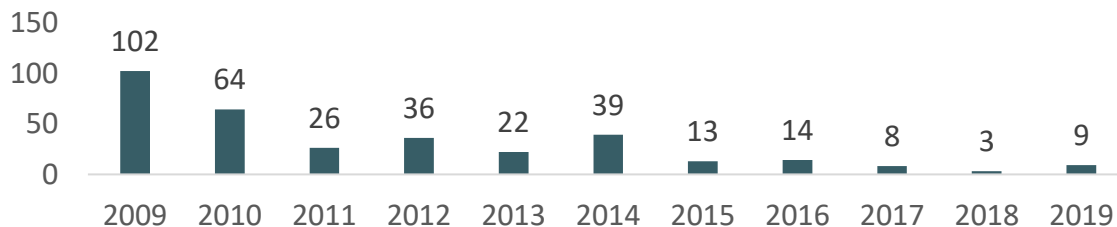
SWEDISH COMPANIES DRIVING CHANGE

Companies that buy in branded products differ slightly from companies with their own brands, when it comes to sustainability work. Even though Stadium for example, has not had any of the chemicals in question in their own brand products, the company assesses that around three percent of other brand products bought in, contain some of them. To further reduce this figure, Stadium works closely with these brands, and Stadium aims to influence the suppliers of these products even though they are a relatively small fish in this context.

PRESENCE OF RESTRICTED CHEMICALS IN LINDEK PRODUCTS

No of products tested that have contained chemicals on the Lindex restricted substance list, 2009-2019.

Please note that the Lindex restricted substance list is based on higher requirements and contains more hazardous chemicals than those covered by the proposed tax.



Source: Lindex

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“A tax ought to drive substitution, but the way it is designed now, it does not take into account how the industry works in practice. It is going to put a brake on the forward leaning work with hazardous chemicals instead.”

– Anna-Karin Dahlberg, Sustainability Manager, Lindex

Major consequences for testing, administration and organisation

Despite the good intentions of the tax, there is a big risk that industry role models on the chemicals issue will also be negatively affected by the tax. Even companies that do not make use of such chemicals will need to allocate significant resources to testing and administration. Adaptations must also be done very quickly, even though lead times are often long.

WIDE-RANGING CRITICISM OF THE TAX STRUCTURE

Despite the fact that the companies interviewed do not make use of the chemicals in question today, a tax of the type the Inquiry proposes would have negative consequences on their business, including in the form of excessive testing and administration.

RISKS LEADING TO EXAGGERATED TESTING

It is common to perform risk-based testing of products and materials today, to check for the presence of undesirable chemicals. This entails a random sample frequency based on how big the risk of the respective chemical being present is. This provides a good overview of the extent to which the chemical is present in the range. Increased demands for testing risks leading to superfluous testing.

ADMINISTRATION INSTEAD OF SUSTAINABILITY

If the Inquiry proposal is passed, there would be an increased need for administration, especially concerning claiming relief against the tax. This would entail increased costs for companies, but also risks requiring extensive investment, such as in new business systems that are adapted to process the tax.

This increased need for administration would also mean significant resources being diverted from sustainability work, especially for smaller companies with limited scope to employ more staff. This risks reducing sustainability work by companies, despite the intention being the opposite. As the chemicals that the tax is aimed at have generally already been phased out within the industry, no benefits would be gained in such cases – either for companies, the environment or consumers.

RAPID IMPLEMENTATION DESPITE LONG LEAD TIMES

The fashion industry generally has long lead times and has very largely already decided on ranges and prices for products that will be sold in 2021. To prevent the chemical tax having greater consequences than necessary for profitability, ranges, prices and processes need to be adapted long before the decision on the tax is taken. As the tax is proposed to come into force on 1 April 2021, significant adaptations to businesses would also need to have been implemented during a period when the Covid-19 pandemic has drastically reduced sales in the industry and 30 percent of employees have been furloughed.

Price increases reduce demand for sustainability

The companies argue that the cost of the tax and the increased testing and administration will almost certainly be added to the retail price to consumers. This means that the products would become more expensive across the board, which in turn, risks leading to more sustainable products being passed over as these are often more expensive.

THE TAX WILL BE EXPENSIVE FOR CONSUMERS

The companies argue that the tax will hit retail prices to consumers as most companies in the industry have low margins. The Inquiry assumes that the tax would be added to the retail price, i.e. the price of a product in store would increase by the amount of the tax on the product. The industry concurs, and argues that the increased cost of administration would also be passed on to consumers.

LESS CHOICE WHEN PRODUCTS BECOME UNPROFITABLE

Products in a limited edition in particular, such as special orders or special materials, risk becoming unprofitable as the costs for testing and administration are the same irrespective of quantity ordered. Several companies say that sometimes, for example when a product consists of many materials, it can even be more economically viable to pay the tax rather than performing all the extra tests and administrative tasks. This would make it more difficult for small and start-up companies to make their business profitable, and to drive innovation.

This will also affect demand in the sense that larger order quantities and bigger companies will be favoured rather than putting a premium on sustainable products, which is the intention behind the tax.

INTERNATIONAL BRANDS WILL DISAPPEAR

Sweden is often a relatively small market for international brands. Many of the international brands that market products in Sweden, either via their own channels or via distributors, would therefore need to perform tests on a large quantity of goods and products even though few of them are sold in Sweden. This risks resulting in certain international brands leaving Sweden, or choosing to pay the tax, whether or not their products contain chemicals.

SUSTAINABILITY A LESSER PRIORITY WHEN GOODS BECOME MORE EXPENSIVE

When goods become dearer in general, consumers need to spend a bigger share of their income on purchases. This means that consumers would become more price sensitive, which in turn, risks leading to more sustainable products being passed over as these often cost more.

Kavat estimates that the price of a pair of shoes costing SEK 500 today, would go up by SEK 50 to 100.

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“At the moment, our suppliers are very familiar with the Reach regulation and know what this entails. Introducing our own Swedish side track where we are going to force suppliers to test their materials for irrelevant chemicals feels both unprofessional and unnecessary. Our partnership with our suppliers is based on a close relationship based on common knowledge about the materials and how they are manufactured, what is added for a certain functionality and so on. The vast majority have tiny margins to make a profit and this means you aim to concentrate on what delivers added value in a business and what keeps the business afloat.”

– Marie Scheidl, CSR Coordinator at Hestra

Sustainable business models are being hindered

Many companies have been actively addressing the issue of chemicals for a very long time, and are now choosing to tackle more and more sustainability challenges. The re-use and recycling of materials risks being hindered by the new tax, however.

HAMPERING BUSINESS MODELS OF THE FUTURE – REUSE AND RECYCLING

The companies interviewed point out that hazardous chemicals have long been a relevant concern in the industry, and that the tax would have been a big help around 20 years ago when the use of these chemicals was widespread. Today, the industry focuses on the more wide-ranging concern of reconfiguring their business models to become more sustainable, such as by reusing clothes and recycling materials.

UNCERTAIN FUTURE FOR KAVAT'S REWORKED SHOES

Kavat now offers its customers a discount on new shoes if they bring in used shoes. These are renovated, such as via resoling and then sold to consumers. In this way, the full usage potential and life cycle of the shoes are utilised, without lowering the quality.

If the chemical tax is passed in its current form, these

shoes would have to be tested for the chemicals concerned before they could be sold without being taxed. As testing of an individual product is not profitable, the consequences would probably be that Kavat would be forced to pay the chemical tax on these shoes. This would mean the price of reworked shoes would increase, which risks making the business model unprofitable and reducing sales of sustainable products.

RECYCLED MATERIALS AND SECOND HAND RESTRICTED TO SWEDEN

The chemical tax would also mean that used clothes from other countries would be taxed. This means that second hand vendors (such as Sellpy) would need to pay tax on the import of second hand garments, which goes against the international business model and what is best for the clothes.



Question marks remain about proof

Clearer guidelines on how proof is provided and what testing is required will be of major importance if the tax is introduced. The Inquiry offers no clear answers as to how tax authority assessments are to be made, which creates great uncertainty for the companies.

CLEARER GUIDELINES ON CERTIFICATION REQUIRED

The Inquiry claims that a certificate from the manufacturer stating that a certain chemical has not been used, will be sufficient proof to claim relief in most cases. However, manufacturer certificates should be assessed from case to case, and will not always be sufficient. Several of the fashion companies raise this as an element of uncertainty with regard to what measures they need to take to avoid being taxed. They also say that it is important that clear guidelines are produced in the event the tax is implemented as the Tax Agency also lacks specialist knowledge in the chemicals area.

GUIDELINES FOR TESTING ARE ALSO NEEDED

Even if the production of evidence will mainly be effected with the aid of manufacturer certificates, a certain proportion of products and materials will need to be tested. The Inquiry states that tests must be done on each homogeneous material in a product. How often each material needs to be tested, and if risk-based testing is permitted, is however unclear. Such unclear guidelines make it very difficult for retailing companies to assess test costs. One of the companies interviewed estimates, for example, that the cost will lie somewhere between MSEK 2 and 29 , an enormous range.

The companies say that it is becoming increasingly common to test for chemicals early in the production process, to ensure that the substances used are approved before production is started. Another grey area in the proposed legislation is therefore whether this type of chemicals check is considered sufficient to claim tax relief, or if tests on finished products will need to be performed in Sweden.

New innovations also lead to new types of testing. One example is Bhive, a company that offers a service where the chemicals stock of a producer is scanned with the help of an app, so the customer can quickly gain an understanding of what chemicals are used. The guidelines that are being developed in case the tax proposal gets passed, ought to take into account that innovations are continuously being made within the chemicals area.

WEIGHT RULES AFFECT THE ADMINISTRATIVE BURDEN

A third unclear aspect is how the weight of products is to be assessed. Several companies say that in cases where garments and shoes in different sizes are taxed differently due to their different weights, the matter of monitoring weight will be particularly demanding on administrative resources.



Measures need to focus on the carrot rather than the stick

A tax on chemicals already phased out risks making employees less motivated to lead the way when it comes to phasing out even more hazardous chemicals.

THE TAX IS SEEN AS NOT TAKING INTO ACCOUNT LONG-TERM CHEMICALS WORK

Several of the interviewees – some of the most knowledgeable and fervent supporters of eliminating hazardous chemicals from our clothing in Sweden – say that they view the proposed tax as a penalty that reduces their motivation to continue their forward looking and visionary work. Over the past few decades, companies in the industry have worked off their own bat in combination with strongly expressed consumer opinion, to gradually eliminate one hazardous chemical after the other.

The companies now feel that their work risks facing a tax that can be perceived as a penalty. By extension, according to modern psychology theory, this can risk passivity in companies that have been seriously addressing sustainability issues for decades, leaving them half-hearted in continuing to phase out chemicals in our clothing.

INTERNAL MOTIVATION THE MOST EFFECTIVE

Motivation theory, that looks at the driving forces that make us act in a smart and efficient way, often divides motivation into internal and external factors. This is based on the theory that drive and motivation are influenced by what consequences follow from the actions we take.

Internal motivation comes from our finding what we do pleasing and meaningful, external motivation can e.g. be receiving rewards in the form of money or that we avoid punishment. Both can be needed to get things done, but from a longer term perspective, internal motivation is considered to deliver better results and more creative and diligent workers. Research also shows that internal motivation can be negatively affected by external motivation factors when these are perceived to be controlling and/or result in negative feedback about a person's competence.

ENCOURAGING MEASURES

Viewed overall, a tax on chemicals that have already been phased out, risks demotivating fashion company employees. The driving force of leading the way in phasing out other hazardous chemicals than those being targeted, can lessen. This undesired side effect could be softened with carrots such as scrapping tax on goods that do not contain the listed hazardous chemicals and to exempt products already certified from having to present proof of such (see more on following slides with proposals for improvements and a change of structure).

The chemical tax structure can be improved

Even though the companies share the tax proposal intentions, the tax entails tangible risks of unintended consequences. If the tax is introduced, extensive amendments to its structure ought to be made, such as exempting products that are part of well-functioning chemicals work, removing the minimum level of 5 percent tax, allow risk-based testing and/or focus on those companies that knowingly include chemicals in their products.

EXEMPT GOODS AND COMPANIES WITH WELL-FUNCTIONING CHEMICALS WORK

Many companies pursue active chemicals work, such as within the parameters of Kemikaliegruppen* or international standards. Exempting these companies from the tax would create more incentives to continue working with the chemicals issue beyond the seven specific substance groups the tax addresses, and thereby creating greater change in the longer term as well. This would also make it easier for companies with smaller resources to work proactively.

Many companies also strive to environment certify their products, such as Kavat that has eco label-certified many of its shoe models. This is an EU label that means the product is sustainable and less harmful for the environment. Making these products tax exempt, would reduce the administration load at the companies without increasing the presence of the chemicals.

ONLY TAX PRODUCTS THAT CONTAIN THE CHEMICALS

The Inquiry's proposal as it is today, means that even products that are free from the chemicals that would be subject to taxation, would face a tax of 5 percent of SEK 40 per kg. This corresponds to a tax of SEK 2 per kg, and SEK 2.5 including VAT. For Stadium for example, this would mean the tax would amount to around SEK 25 million per year, which corresponds to MSEK 31 including VAT. Removing this part of the tax would increase the incentives to look to eliminate other hazardous chemicals.

ALLOW RISK-BASED TESTING

Many companies work with risk-based testing, which means that high risk materials are tested more often. The H&M Group has, for example, been involved in developing the AFIRM test matrix in their Restricted Substances List for 2020, that sets out how often different materials ought to be tested for each respective substance.

Permitting this way of testing materials would reduce costs, and at the same time avoid unnecessary testing. Ensuring that the work done by the companies on chemicals is largely taken into account, especially in terms of how well chemicals used in production are checked and restricted (input control) would be even better when it comes to general environmental gains, however.

FOCUS ON COMPANIES THAT KNOWINGLY USE THE CHEMICALS

The reason why the chemicals concerned are added to products, is that they fulfil a function, such as repelling dirt. Products that contain these chemicals can therefore be marketed with specific product qualities, which ought to enable the company to charge a price premium to finance the chemical tax. Targeting the tax at products where the chemicals concerned are intentionally used, would therefore make a bigger difference, and reduce the burden of proof problem.

*Kemikaliegruppen (The Chemicals Group) is a network and part of The Research Institute of Sweden, RISE, that aims to communicate knowledge on chemical and environment-related issues to its member companies in the textiles and electronics industries.

Possible solutions other than tax

Even though tax has the advantage of raising money for government coffers, this places an extra administrative burden on companies, and an opportunity to buy their way out. In order to reduce the presence of hazardous chemicals, a ban at national or EU level, greater powers for the Swedish Chemicals Agency and a bigger focus on future challenges, are accordingly other possible solutions to improve access to sustainable clothing.

ACCELERATE REACH

The companies praise the Reach regulation as a good example of chemical legislation. As the fashion industry is global, international agreements are the easiest way to work to achieve change in the whole industry. Sweden introducing its own chemical tax paves the way for more special legislation among the EU countries, which would undermine trade.

However, within Reach, a substance can be on the list of candidates for banning for a long time, and accelerating this process could therefore be one way of achieving more rapid change.

SWEDISH CHEMICALS AGENCY WITH MORE TEETH

The Swedish Chemicals Agency is a public authority that possesses expertise within the environment and chemicals area. Expanding the Agency's inspection powers could be one way of accelerating efforts to eliminate harmful chemicals from products.

BAN HAZARDOUS CHEMICALS

Many companies stress that a ban on the chemicals in question would only affect around 16 percent of products that actually contain these chemicals. As the companies that have engaged in extensive chemicals work, probably do not use any of the chemicals today, they should not be impacted. A ban would mean that companies that have not addressed the issue would be forced to adapt, instead. Many fashion retailers argue that a chemical tax risks becoming a half measure where companies that do use the chemicals feel it is OK to pay the tax and continue as before.

FOCUS ON THE CIRCULAR BUSINESS MODELS OF THE FUTURE

In July 2020, the government resolved on a new strategy with a focus on the circular economy. The aims of circular business models are very much on the agenda within the clothing and footwear industry, and a big focus for companies on the retailing side. If the chemical tax were introduced in its present form, this risks having negative consequences for the second hand and recycled materials market, however. An environment tax on fashion ought therefore focus on encouraging efforts to address the sustainability challenges that are more urgent for companies today instead, such as reconfiguring to circular business models.

Summary: Good intentions but structure less good

THE INDUSTRY SHARES THE TAX INTENTIONS

The clothing and footwear industry has long worked proactively to eliminate hazardous and environmentally harmful chemicals from their production. None of the companies interviewed, Kavat, Hestra, H&M, Lindex and Stadium, therefore uses the chemicals that the tax is aimed at today in their own products.

THE TAX STRUCTURE PUTS SUSTAINABILITY AT RISK

The tax risks leading to negative consequences for the companies interviewed, such as the need for excessive testing and additional administration. As this will increase the retail price to consumers and drain resources from other sustainability work, the tax risks companies having to cut back on sustainability efforts. What's more, the tax would also apply to reused clothing, which goes against the circular business models that companies within the sector today are seeking to put in place.

CLARIFICATION AND AMENDMENTS VITAL

There is still a great deal of uncertainty as to how the evidentiary requirement in the tax issue should be resolved, if the tax comes into force. However, it is clear that the structure of the tax has potential to be improved, and that other solutions are available for how the issue of chemicals and environment can be tackled.



None of the companies interviewed, Kavat, Hestra, H&M, Lindex and Stadium, uses the chemicals that the tax is aimed at today in their own products.

06 | Experiences from the chemical tax on electronics

Reflections on what has gone before

Chemical tax on electronics since 2017

The chemical tax on electronics was introduced in 2017 and is similar in design to the proposed tax on clothing and footwear. Like the proposed chemical tax on clothing and footwear, it is based on weight, and there is scope for tax relief of up to 90 percent.

CHEMICAL TAX ON ELECTRONICS SINCE 2017

From 1 July 2017 a specific duty has been levied on electronics goods. The aim of the tax is to contribute to the national environment goal of a toxic free environment, and that this should be effected by reducing the presence, spread and exposure to hazardous flame retardants. The chemical substances that are primarily intended to be phased out are Bromine, Chlorine, and Phosphorus Compounds, which to a greater or less extent, are found in all types of electronics goods, especially circuitboards.

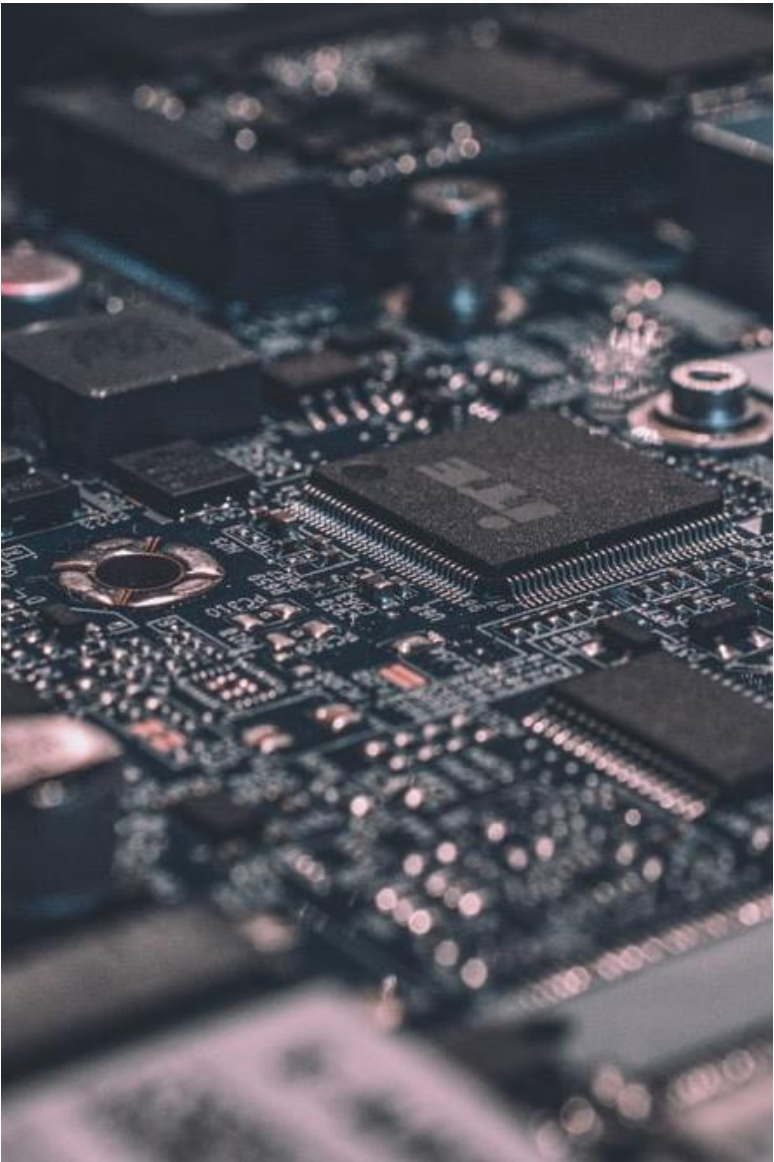
GAINS FOR THE ENVIRONMENT AND HEALTH THE MOTIVE BEHIND THE TAX

The government inquiry that lay the grounds for the introduction of the chemical tax (SOU 2015:30) predicted major gains for the environment and health, annual tax revenues of SEK 2.4 billion and a 4.5 percent reduction in sales of electrical goods per year. The head of the government inquiry also predicted that 0.4 percent of retail sales of electrical goods to Swedish consumers would be switched to international and untaxed e-tailing.

The tax rate was raised in August 2019 and from then on is to be increased each year in line with the consumer price index. The tax levels for 2020 are shown in the table below.

	Tax
White goods	SEK 11/kg
Other taxable products	SEK 163/kg
Maximum tax amount	SEK 448/ product

As the tax is based on the weight of the product, it affects different types of products differently. For example, the tax on mobile phones is very low, while TV sets are often subject to the maximum tax amount. It is possible to gain tax relief up to 90 percent in cases where it can be proved that the product meets the requirements concerning bromine, chlorine and phosphorus compounds.



Foreign e-tailers have benefited

The chemical tax on electronics differs from the proposed tax on fashion as foreign companies have been tax exempt to date. The electronics tax also has a maximum limit per product.

FOREIGN COMPANIES AVOID TAXATION

The chemical tax on electronics has been criticised for creating significant competitive disadvantages for the Swedish electronics industry as private importers via e-tailing are not taxed. In March 2020, the government submitted a referral to the Council on Legislation with a proposal to eliminate the exemption for foreign retailers. In which case, the tax liability would be structured in the same way as the tax liability for the chemical tax on clothing and footwear. The amendment is proposed to come into force on 1 October 2020.

MAX AMOUNT ON ELECTRONICS

One difference in the structure of the tax on electronics and the proposed tax on clothing and footwear is that the tax on electronics has a maximum limit. The maximum tax amount per product in 2020 is SEK 448, which corresponds to a white goods product that weighs 40 kg or another electrical product that weighs 2.75 kg.

BETTER CASH FLOW WITHIN E-TAILING

Companies that have been approved as stockists, are liable to pay tax in the month after goods have left stock and been supplied to stores. In the case of e-tailing, as a rule, the goods are shipped straight from a warehouse, whereby in practice the tax liability is triggered in association with delivery to the customer, and the tax is payable the following month. This gives the e-tailer a certain competitive advantage from a cash flow perspective, as the company does not, as a rule, need to disburse any money.



Job losses and lower than expected revenues

Revenues from the electronics tax have been significantly lower than the inquiry originally estimated.

REVENUES ONLY 60 PERCENT OF EXPECTED AMOUNT

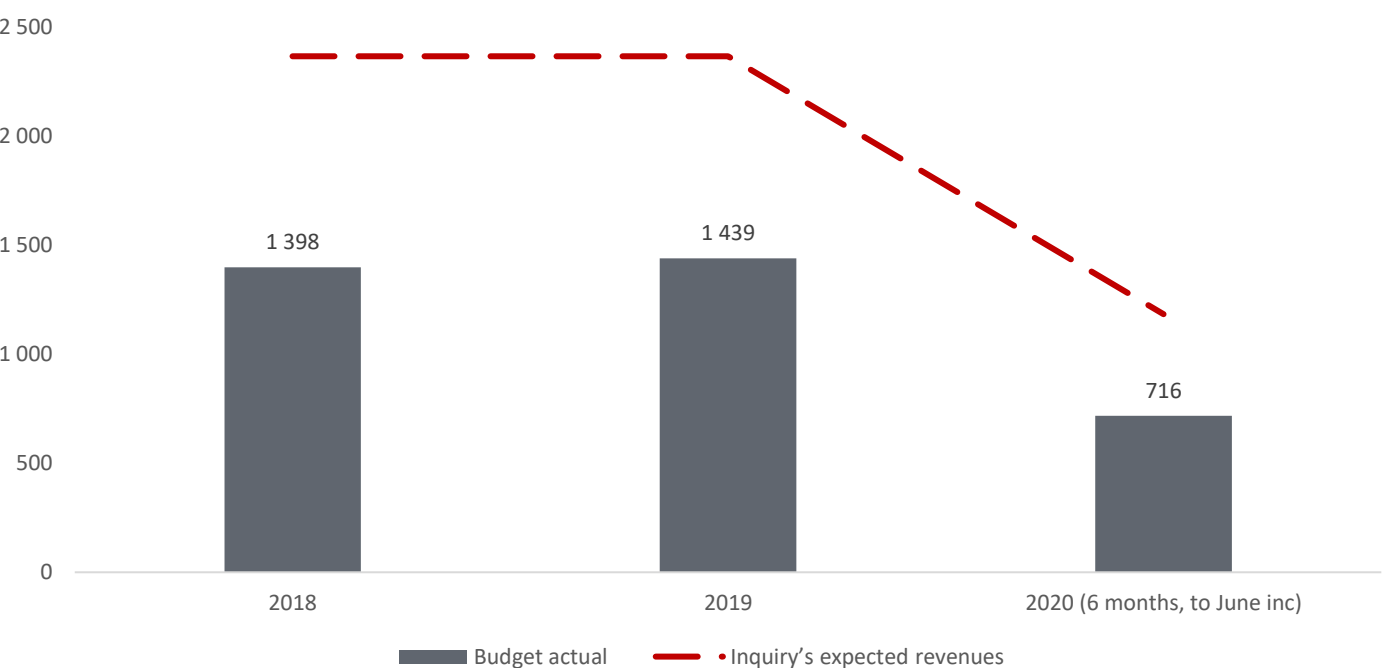
The inquiry that lay the grounds for the chemical tax on electronics (SOU 2015:30) predicted that the tax would generate annual revenues of around SEK 2.4 billion gains for the environment and health, annual tax revenues of SEK 2.4 billion. Actual revenues have proved to be approx. 60 percent of the budgeted figures per year over the first two full years, and this trend seem to be continuing in 2020.

JOB LOSSES AND A ZERO SUM GAME FOR THE GOVERNMENT

As a consequence of the negative effect on sales that the tax had, the home electronics sector generates less VAT income than would have been the case if the tax had never been introduced. The same applies to lost income tax and company tax. In previous analyses, HUI has noted that lower than expected gross revenues combined with the above negative effects, along with increased costs for public authority administration, have probably made the chemical tax on electrical goods a zero sum game for government finances. At the same time, the tax is assessed as have an negative effect on employment in the electronics sector and reduced the number of jobs by the equivalent of between 800 and 2,000 full time jobs.

EXPECTED AND ACTUAL TAX REVENUES

Expected and actual tax revenues for years 2018-2020, MSEK



Source: ESV, SOU 2015:30

The purchase journey looks different within electronics and fashion

Consumption of home electronics and fashion differs in several ways. Electronics goods are more homogeneous and comparable, which means consumers put a greater focus on price and technical specifications than when buying clothes and shoes. Women, who are generally more environmentally conscious than men, are over represented when it comes to clothing and footwear consumption. This makes it easier for clothing and footwear retailers to compete on things other than price, which drives stronger self-regulation within the fashion industry than within home electronics retailing.

ELECTRONICS PRODUCTS ARE MORE HOMOGENOUS

Customers often need to try on clothing and footwear to check they are the right fit, size and quality. Electronics goods are standardised to a greater extent and choice is determined by technical specifications, product reviews and assessments, while choice of fashion product is largely based on subjective opinions about the design and material for example. This reduces comparability between products within fashion retailing and increases the opportunity to attract consumers with different types of “soft ” competitive advantages, such as eco friendly materials.

HIGH COMPARABILITY – HIGH PRICE SENSITIVITY

As electronics products are often homogeneous, it is easy to compare prices between retailers and between products, which increases price sensitivity and where consumers hop more between suppliers. This also reduces a company’s scope to compete with other types of advantages, such as more sustainably produced products. Within fashion retailing, comparisons are made to a greater extent at category level, such as pants, than for a specific product. This means it is easier for a consumer to substitute one pair of pants for another pair due to parameters other than price. Price comparisons for specific brands can, however, be made between countries and consumers can make a purchase decision depending on where the best price and delivery terms are offered.

WOMEN OVER REPRESENTED WHEN IT COMES TO CLOTHING AND FOOTWEAR CONSUMPTION

Within electronics retailing, men account for the majority of consumption, while the opposite is the case within clothing and footwear retailing. Previous surveys, such as the Svensk Handel Sustainability Survey in 2018, show that women to a greater extent think it is important that the products they consume are sustainably produced. This helps to suggest the clothing and footwear retailing sector probably offers more fertile soil for self-regulation in the environment area.

Electronics	Clothing and footwear
Homogeneous products	Heterogeneous products
Greater price sensitivity	Lower price sensitivity
High proportion of informed purchases	High proportion of inspirational purchases
Higher comparability	Lower comparability
Men over represented as consumers	Women over represented as consumers

E-tailing and sustainability differentiate the sectors

Foreign purchases account for 12 percent of e-tailing within both fashion and home electronics. However, e-tailing for home electronics is primarily driven by price, while fashion consumers search for new types of products outside the country. Demand for sustainable products is higher within fashion.

12 PERCENT OF PURCHASES ARE MADE ABROAD

Foreign purchases within the fashion and electronics sectors respectively account for a similar share of total purchases. According to E-barometern from PostNord, 12 percent of purchases are made within these categories from foreign online stores. The electronics sector is more digitally mature however, and a larger presence on the internet, in terms of value. Foreign purchases within electronics retailing is very largely price driven, while international fashion retailing is driven by consumers looking for products that are not found on Swedish websites.

DIFFERENT CHALLENGES WITHIN E-TAILING

The barriers to entry for foreign trade look somewhat different in both sectors. Within fashion retailing, international e-tailing requires a credible system for simple returns if the products are not what the consumer wants. Simple returns are also of the utmost important as ordering the same product in several different sizes and/or colours to try at home before

sending back some of the garments, is a widespread phenomenon.

Clothes are not bulky, however, which means they are light and relatively cheap to ship between countries. Within the electronics sector, the biggest barrier is that certain products such as TV sets and fridges are large and bulky, which makes delivery more complicated.

SUSTAINABILITY EXPECTATIONS HIGHER WITHIN FASHION

Consumers impose higher sustainability demands within fashion retailing than within electronics. These high consumer demands have, together with the fact that clothes and footwear are worn close to the body and so expose the body to their contents to a greater extent than electronics products, meant that the sector has been driving development towards more sustainably produced products for a long time.



MOST POPULAR E-TAILING COUNTRIES

Percentage of foreign consumers that have bought products online from the respective country.

Clothing and footwear		Home electronics	
UK	30%	China	37%
Germany	17%	Germany	19%
China	15%	UK	15%

Source: PostNord/HUI, E-barometern, 2019.

Summary: Economy harder hit than the chemicals

DISAPPOINTMENT FOR GOVERNMENT FINANCES

The electronics tax shows that there are major question marks surrounding the financial consequences a chemical tax as currently proposed risk giving rise to. The electronics tax has not generated the revenues expected, which has resulted in the tax becoming a zero sum game for the government while at the same time jobs have been lost.

WATCH OUT FOR MARKET DISTORTIONS

Another lesson from the chemical tax on electronics is that the tax effects on the competition situation ought to be reviewed. The electronics tax has distorted competition in favour of foreign and online companies, which ought to be born in mind in the event a chemical tax on clothing and footwear is introduced.

FASHION INDUSTRY HAS A CLEARER SUSTAINABILITY PROFILE

The fashion industry and home electronics industry differ in several ways. The clothing and footwear industry has a lower proportion of e-tailing, less price sensitive products and more environmentally engaged consumers. This has led to the Swedish fashion industry actively profiling itself within sustainability, which means that regulations concerning chemicals need to give greater consideration to what is already being done within sustainability in the fashion industry compared to the electronics sector.



07 | Conclusions

900 jobs lost – environment gains unknown

The combined picture is that the chemical tax rests on shaky grounds as it lacks genuine socio-economic justification. It is clumsily constructed and legally uncertain, the environment benefits are unknown and resources will be drained from existing sustainability efforts.

KEY NEED TO SUPPORT EVIDENCE-BASED SUSTAINABILITY WORK

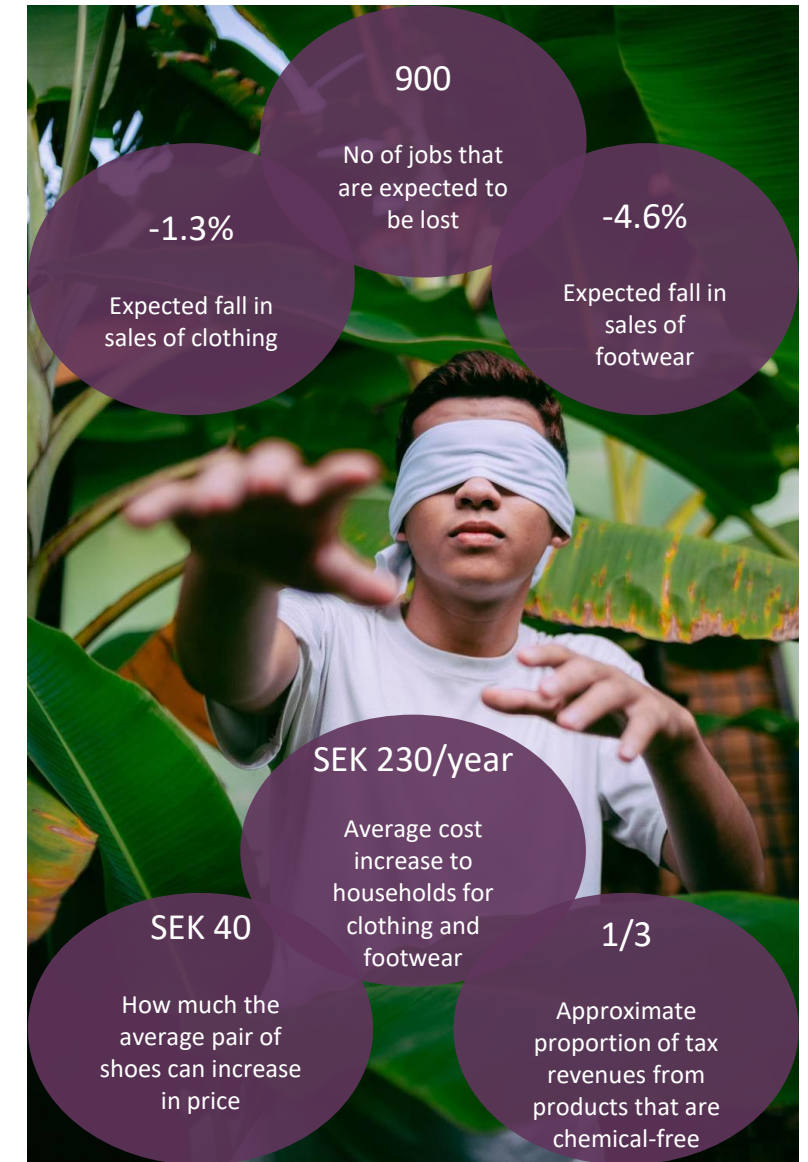
Swedish fashion companies engage in extensive chemical work and lead the way globally when it comes to sustainability issues. They do not oppose the use of political instruments in general, but the measures that are taken are expected to be well-considered and highly appropriate. The current proposal is unanimously viewed in the industry as legally uncertain, cost driving and counter productive as it will hinder existing sustainability work and is difficult to quantify.

CLEAR COMPETITIVE DISADVANTAGE FOR SWEDEN

Fiscal measures that sharply increase the costs burden for companies should always be solidly based on firm scientific and socio-economic grounds. This especially applies at a time like now when we are all facing tremendous uncertainty as a consequence of the ongoing pandemic and global financial crisis. Its legitimacy will be weak if many jobs and companies are put at risk while at the same time, the policy proposal lacks a clear upside.

ENVIRONMENTAL EFFECTS UNCERTAIN, COSTS KNOWN

It is a case of uncertain environment effects versus obvious costs that, depending on how the legislation is applied, can be very extensive for consumers and companies. For example, 900 jobs will be at risk and household costs for clothing and footwear will increase by SEK 230 a year despite lower consumption. The tax is expected to have a negative impact of 1.3 percent on sales of clothing and 4.6 percent on shoes, which will make recovery in the wake of the Coronavirus crisis more difficult. Many companies in the sector are keen to minimise the presence of hazardous chemicals, but regulation without demonstrable health and environment benefits that at the same time entail very extensive downsides, risks undermining confidence in environment policies. Reversing the “burden of proof” in practice and a basic tax on all goods irrespective of their chemical content, are examples of elements that put big question marks against the legitimacy of the structure. A closer look at the proposal in its current form shows that however the tax is applied, companies will face a big administrative load without any benefits, as the chemicals concerned are often not present in product ranges or already being phased out in line with EU Reach regulation and self-regulation by companies.



Tax a dubious instrument for the purpose

The choice of tax as an instrument, is difficult to reconcile with the overall goal of a “toxic free environment”. Taxation is potentially appropriate to achieve socio-economically optimal use, but other methods are more likely to achieve a total phase out quicker.

UNKNOWN EXTERNALITIES IMPOSSIBLE TO CORRECT

The proposed chemical tax cannot be justified based on socio-economical considerations as it, as SOU 2020:20 sets out, lacks supporting data to assess possible health and environmental gains from taxing the chemicals in question. At the same time, it is clear that the costs of taxation will be significant for consumers and companies.

GOAL AND INSTRUMENT AT ODDS WITH EACH OTHER

When it can be assumed that the external effects are known, taxation tends to be favoured ahead of alternative methods. If, on the other hand, legislators consider that, *despite the lack of socio-economic justification*, there are still grounds to adopt obstructive measures, one proceeds in accordance with a kind of precautionary principle, that would rather motivate a ban. This can be the case if there is reason to suspect that the cost of health problems can be very high for a small number of individuals (risk of death or serious disease), and at the same time the cost of the ban itself in the form of loss of consumer benefits, can be spread over millions of people.

ENVIROMENTAL POLICY MUST MAKE A CHOICE

To the extent that policy goals take precedence over the total welfare effect – for example the environment policy aim of a toxic free environment – a ban would seem to be a more logical measure than taxation. For example, gross violations of rights are not taxed. They are banned instead as such violations are never deemed to be able to be justified by calculating the benefits. The use of duty as an instrument when the goal is to totally eliminate a phenomenon (such as the presence of certain chemicals), comprises a strange approach as either the inconsistency between aim and means is revealed, or alternatively that there are other incentives that play a part in the process and that suggest the taxation alternative. If the latter is the case, it is of importance that there is transparency as to what these supplementary goals are. The fiscal incentive is particularly worth mentioning in this context as the wish to collect tax can sometimes be in direct opposition to the environment benefits. We say this as there are certain driving forces among public authorities not to erode the tax base – in other words, not to eliminate in practice those phenomena that are assumed to cause environment damage.



The companies: Good intention – poor design

Companies in the clothing and footwear industry have been working long and hard to phase out hazardous chemicals from their production. As currently designed, the tax would therefore entail resources being transferred from existing forward looking sustainability work to administer a tax that would have a very limited effect. This creates a need to adapt the measures proposed to the current situation and what is being done within the industry.

THE TAX RISKS REDUCING SUSTAINABILITY WORK

The clothing and footwear industry has a long tradition of working with sustainability issues, including by excluding hazardous chemicals from their production. None of the companies interviewed in association with this report (Kavat, Hestra, H&M, Lindex and Stadium) uses any of the chemicals that the tax concerns, in their own products.

The chemical tax on clothing and footwear will, in its proposed form with reversed burden of proof, entail significant costs for companies in terms of tax, VAT, administration and increased testing. In turn, this brings a big risk that resources will be switched from the sustainability work being pursued today, to administer and cover the costs of the chemical tax. As the chemicals concerned are largely not used by the companies with a serious and ambitious sustainability agenda, such a transfer of resources would have a negative impact on sustainability work, with associated consequences for both companies, consumers and the environment.

PROPOSALS FOR IMPROVEMENTS

The companies interviewed in this report have made several suggestions as to how legislators could work to reduce the presence of hazardous chemicals, and at the same time benefit other sustainability work being pursued by the companies. These proposals include to:

- Exempt companies and products where chemical work is actively pursued within the parameters of national and international standards and certifications.
- Ban the specified chemicals instead of introducing a tax on them.
- Only tax products that contain the specified chemicals.
- Permit risk-based testing
- Focus on supporting circular business models of the future.

Please read more about these proposals on slides 39-40 of the report.



