

Financial Incentives to Grow the Circular Economy

Wildlife and Countryside Link (Link) is the largest environmental coalition in England, bringing together 86 organisations to use their joint voice for the protection of the natural world.

The UK has an enormous opportunity to benefit from growing the circular economy: it could create almost half a million British jobs by 2035.¹ But without the right incentives for UK businesses and consumers, it risks getting left behind market leaders like the Netherlands.²

We are currently overconsuming resources beyond what is healthy and sustainable for the planet, with the UK living beyond its planetary means.³ However, the adoption of a circular economy – where virgin resource use is minimised and what we do use is kept in circulation for as long as possible – can deliver environmental, economic and social benefits. To deliver these benefits and its manifesto promise of a “zero waste” society the Government will need new financial incentives to promote a circular economy and reduce waste.

This paper highlights three policies in three areas that can be deployed quickly and would have the greatest impact in growing the circular economy. (1) Reforming current policies: enhancing the current extended producer responsibility (EPR) scheme. (2) Driving change in business practices: making finance easily available for circular economy innovation. (3) Encouraging consumer behaviour shifts: VAT reduction on circular economy products and services. It focuses on cross-sector measures, rather than measures specific to industries. An annex details further policy options beyond the priority policies described in detail.

Reforming current policies: EPR schemes fit for the future

A review of the evidence on circular economy incentives found that levelling the economic playing field between products following a linear economic model and products that minimise use of virgin materials is one of the most important drivers for expanding the circular economy.⁴ EPR places the costs of the negative externalities of waste generation directly on producers. This has the potential to incentivise the consideration of a full lifecycle approach to the product value chain and tackle both the upstream and downstream impacts of production. This will reduce the impact of resource extraction and processing and enable reuse and recycling of materials.⁵ However, current EPR proposals for packaging, and consultations on waste electricals and electronic equipment (WEEE), have not accounted for circular economy

¹ https://green-alliance.org.uk/wp-content/uploads/2021/11/Levelling_up_through_circular_economy_jobs.pdf

² <https://www.circle-economy.com/blogs/the-circular-economy-who-is-leading-the-way>

³ https://www.wwf.org.uk/sites/default/files/2021-06/Thriving_within_our_planetary_means_full_report.pdf

⁴ <https://eitrawmaterials.eu/wp-content/uploads/2020/07/EIT-RawMaterials-project-POLICE-Final-report.pdf>

⁵ <https://op.europa.eu/en/publication-detail/-/publication/51378e0a-d303-11eb-ac72-01aa75ed71a1>

approaches beyond recycling. Our proposal to go further and faster on EPR would spur innovation and maximise the impact of the policy.

- **Current policy:** Packaging Extended Producer Responsibility (pEPR) measures are due to commence from January 2025. In preparation for this, in-scope businesses have been required to report their packaging data from April 2024. Modulated fees will be introduced from year 2 of the policy.
- **Our proposal:**
 - **Accelerate the expansion of EPR to new sectors:** although single-use packaging epitomises the linear economy, all products made from virgin materials that end up as waste constitute wasted resources, an impact on the environment, and a missed chance to generate jobs putting the resources back into circulation. EPR should be progressively expanded to other product types, starting with those that cause most harm when they end up as waste. Batteries and electronics can be particularly toxic and hazardous and yet contain precious metals that can be reclaimed.⁶ The textiles industry produces 4.2% of all municipal waste in England and 4-8% of all global greenhouse gas emissions and yet globally only 1% of the materials used to produce clothing is recycled back into clothing.⁷ The UK should follow countries such as the Netherlands, which is planning to introduce EPR across multiple sectors or France which has multiple EPR schemes spanning industries from textiles to vehicle tyres.^{8,9} This will mean innovation and investment in circular practices that minimise EPR fees and that have the potential to drive domestic industries for reuse, repair, refurbishment and recycling. For example, The Business of Fashion estimates by 2025 the global resale market for clothing will reach \$57 billion, up from \$27 billion in 2021.¹⁰ However, the fashion industry is worth over \$2 trillion so incentives such as EPR are needed to shift the economy towards circular alternatives.¹¹
 - **Increase the ambition for modulated fees:** placing lower fees on products that have a lower environmental impact places the burden of negative externalities fully on producers and therefore drives investment in lower impact products.¹² The initial focus of modulated fees for pEPR will be on recyclability, but modulated fees can capture much wider impacts. This will encourage producers

⁶ <https://www.circularonline.co.uk/wp-content/uploads/2024/07/CIWM-373-Batteries-Report-Document-Final-upload-compressed.pdf>

⁷ <https://www.gov.uk/government/publications/waste-prevention-programme-for-england-maximising-resources-minimising-waste/the-waste-prevention-programme-for-england-maximising-resources-minimising-waste#textiles>

⁸ <https://www.rijksoverheid.nl/onderwerpen/circulaire-economie/documenten/beleidsnotas/2023/02/03/nationaal-programma-circulaire-economie-2023-2030>

⁹ <https://journals.openedition.org/factsreports/6557>

¹⁰ <https://www.businessoffashion.com/reports/retail/the-future-of-fashion-resale-report-bof-insights/>

¹¹ <https://www.mckinsey.com/industries/retail/our-insights/state-of-fashion-archive#section-header-2022>

¹² <https://op.europa.eu/en/publication-detail/-/publication/51378e0a-d303-11eb-ac72-01aa75ed71a1>

to consider the life-cycle impacts of their products and lead to growth in sectors which encourage returning materials to the economy. Examples include:

- Reusable packaging should continue to be eligible for no fees supported by tracking the number of reuse cycles required for a given item to ensure it meets the “break-even” point versus its single-use equivalent.¹³
- In the electricals and electronics sector, fees could be modulated favourably for a multitude of product alterations, such as repairability, durability, energy efficiency, and disassembly potential.
- A fashion industry group has led research on how fees could be modulated for textiles, including for durability, undertaking repairs, reselling used items, and recycled content and recyclability.¹⁴
- EPR fees could be increased for the use of chemicals known to be harmful to humans and nature, such as PFAS, Bisphenols, and flame retardants, where there are proven alternatives. Transparency about chemicals used in products and tracing of chemicals in the supply chain is necessary to make this possible. This will increase recyclability, as it is often hard to remove harmful chemicals during recycling, and reduce the risk of leakage of harmful chemicals into the environment.
- Greenhouse gas emissions and other environmental impacts associated with producing a replacement product could be incorporated into EPR.
- **Invest EPR fees in the circular economy:** fees from EPR should be ringfenced to invest in mainstreaming circular practices. Currently pEPR fees will rightly go to local authorities to pay for the cost of collecting and disposing of packaging. As EPR is expanded to cover more sectors and broader impacts beyond the cost of disposal, fees should be invested back in circular economy sectors. For example, fees could contribute to the financing needed to kickstart the circular economy outlined below. This would help industries innovate, and transition to products and practices with a lower environmental impact.

Case study

France’s EPR for waste electrical and electronic equipment (WEEE) includes extensive modulation of fees to increase product lifespan, reusability and recyclability and reduce environmental impact. For example, making spare parts available for a significant time after sale reduces EPR fees, while presence of toxic materials that reduce recyclability increase EPR fees. This has led to a consistently high recycling and re-use rate of 80%.

Source: <https://bestpractices-waste-med.net/>

¹³ The break-even point is the minimum number of uses necessary for a reusable item to be preferable to a single-use item, factoring in all environmental impacts measured within the life cycle analysis.

¹⁴ <https://weft.org.uk/>

Driving change in business practices: financing the growth of the circular economy

Finance markets are already waking up to the value of the circular economy. The number of public market funds with a circular economy focus went up from 1 in 2018 to 10 in 2020, while the number of private market funds with a circular economy focus increased tenfold from 2016 to 2020.¹⁵ However, to accelerate growth of circular economy sectors, further finance is needed. A review of the evidence on incentives for the circular economy found high upfront investment costs are a key barrier to expansion of circular economy businesses.¹⁶ Expanding investment in the circular economy also complements EPR as it helps businesses develop circular alternatives to wasteful practices. We propose both an expansion of Government financing of research into new circular economy processes and crowding in of private finance to businesses in the sector through strategic investment.

- **Current policy:** to date, Government has provided very little direct funding for the circular economy. The waste prevention programme for England: Maximising Resources, Minimising Waste included very small amounts of funding, mostly for very early-stage research projects or demonstrators. This funding is not on the level needed to scale up the circular economy and other countries are pushing ahead. Between 2016 and 2020, the EU invested €10 billion in the transition to a circular economy.¹⁷
- **Our proposal:**
 - **Expand grant funding for circular economy R&D:** while past and current funding for research and development into new ways to increase re-use, recycling, repair and resource efficiency are welcome, they are not enough to transform our economy from linear to circular. For example, some policies identified in the Government's Unlocking Resource Efficiency programme require the development of completely new technologies, such as the ability to sort and extract concrete waste for recycling into new concrete.¹⁸ Innovation funding also has the ability to grow the use of emerging technologies, such as transforming grass cuttings into sustainable bio-based products, such as biofuel, biochar, and peat-replacement as part of a circular economy for organic materials. A project funded by the Department for Transport ("Greenprint") is currently trialling innovative approaches to cutting road verges that benefits biodiversity and seeks to produce biochar from the cuttings.¹⁹ R&D funding could also advance research on limiting the loss of key resources, such as

¹⁵ <https://www.ellenmacarthurfoundation.org/financing-the-circular-economy-capturing-the-opportunity>

¹⁶ <https://eitrawmaterials.eu/wp-content/uploads/2020/07/EIT-RawMaterials-project-POLICE-Final-report.pdf>

¹⁷ https://commission.europa.eu/publications/report-implementation-circular-economy-action-plan-1_en

¹⁸ <https://www.gov.uk/government/publications/unlocking-resource-efficiency>

¹⁹ <https://www.gotolocal.co.uk/2024/04/22/cutting-edge-project-grows-with-grass-collection-trials-in-parts-of-west-sussex/>

nitrogen, into the environment, reducing waste and pollution.²⁰ By investing grant funding in early stage research, the Government can help create the circular technologies of the future and British jobs.

- **Crowding in private finance to growing sectors:** according to research from the European Institute of Innovation and Technology, “policy support is needed to help innovations bridge the 'valley of death' between research funding and commercialization” and grow into thriving business sectors.²¹ Due to entrenched linear economy practices and supply chains, circular economy businesses face high up-front investment costs to compete. The government should provide affordable finance to circular economy businesses to scale up. By investing at an early stage, this will reduce the risk for private investors by allowing businesses to start generating returns, giving confidence to private markets. This will lead to a crowding in of private investment alongside government investment. The Government already has a vehicle it can use to invest in scaling-up circular economy technology and processes in the form of the National Wealth Fund. The UK Infrastructure Bank had waste as a priority sector and this should be broadened to focus on opportunities across the circular economy. This will drive growth, as well as combatting climate change and reducing the environmental impact of linear production. Private finance for the circular economy is growing: in 2023 investments in the UK exceeded £1.3bn.²² However, this pales in comparison to the \$742 billion invested worldwide in fossils fuels alone in 2021. Investing now has the potential to create viable new sectors that can attract additional private investment and grow the economy sustainably.
- **Non-financial support for circular economy businesses:** supporting growing sectors is not just about money, but also the sharing of knowledge and the forging of connections between circular economy businesses. The Government should set up a circular economy accelerator platform that is free to use, shares advice with circular economy start-ups and connects them to research networks and peers. This has been used to great effect by the Netherlands with their Versnellingshuis accelerator which has helped numerous businesses scale up.²³

²⁰ <https://news.mongabay.com/2024/01/agricultural-nitrogen-pollution-is-global-threat-but-circular-solutions-await/>

²¹ <https://eitrawmaterials.eu/wp-content/uploads/2020/07/EIT-RawMaterials-project-POLICE-Final-report.pdf>
pg.23

²² <https://resource.co/article/uk-circular-economy-investments-rose-over-13bn-2023>

²³ <https://versnellingshuisce.nl/praktijkverhalen>

Case study

The EU's LIFE programme for funding environment and climate action invested €948 million in projects contributing to the circular economy between 2014 and 2020. This funded projects including LIFE-ECOTEX, which created a sustainable solution for recycling polyester waste into new raw material for clothing. Companies in the textile, automotive and packaging industries are now working with the project coordinator to commercialise the process.

Source: https://cinea.ec.europa.eu/publications/disrupting-linear-model-life-and-circular-economy_en

Encouraging consumer behaviour shifts: boosting circular businesses through VAT reduction

While focusing incentives upstream on business is essential to transforming business models and practices, measures can also support consumers to transition towards a circular resource use model. While behaviour change campaigns and labelling have their place, they must be backed-up by market-based incentives which allow consumers to benefit financially from engaging in circular practices.²⁴ At a time where financial pressures are high, these measures could also lower household bills. Changes to VAT are some of the simplest ways to alter prices for consumers and encourage more sustainable practices. Multiple parliamentary reports have called for changes to VAT that promote a circular economy.^{25,26} We propose a reduction in VAT on certain products and services that increase the life cycle of products and promote reuse.

- **Current policy:** currently there are few VAT reductions specifically for products and services that encourage circularity. In fact, some applications of VAT discourage reuse and repair. For example, there is currently 20% VAT on retrofit, refurbishment and renovation of buildings but new build has a 0% VAT rate. This drives use of virgin materials instead of keeping existing resources in circulation.
- **Our proposal:**
 - **Reduced VAT on products that facilitate reuse and repair:** currently there is little financial incentive for the consumer to repair a product or keep an existing

²⁴ <https://op.europa.eu/en/publication-detail/-/publication/51378e0a-d303-11eb-ac72-01aa75ed71a1>

²⁵ <https://committees.parliament.uk/publications/3675/documents/35777/default/>

²⁶ <https://committees.parliament.uk/work/170/electronic-waste-and-the-circular-economy/publications/>

one in use for longer. For example, the consumer group Which? noted to the Environmental Audit Committee that buying a new smartphone can be cheaper than having one repaired.²⁷ Although there are multiple drivers behind these costs, reducing VAT on parts and products that facilitate repair and likewise on second-hand products would help tip the balance in favour of longer product life-cycles and, in the case of construction, level the playing field vs. new build.

- **Reduced VAT on repair and sharing services:** in addition to costs for parts and products that facilitate reuse and repair there is also a service cost, such as the labour for repair, which incurs VAT. VAT is also levied on sharing services, such as car sharing. Reducing VAT would promote these services that drive growth in the circular economy. Repair services, in particular, are often labour-intensive. There is therefore potential for the creation of high-skilled jobs in the UK as repairs are usually completed locally. For example, the retailer Currys employs 1,000 technicians in its repairs lab in Nottinghamshire.²⁸
- **Ensuring fiscal neutrality:** reducing VAT on products and services as described will inevitably lead to a reduction in VAT tax take. However, this measure should not be viewed in isolation but as part of a broader system of tax reforms shifting the burden of taxation from circular resource use to virgin material use. For example, VAT reforms can be complemented by taxes on the use of environmentally damaging materials (see case study). VAT cuts would also stimulate economic activity and jobs growth, increasing tax take in other areas.²⁹ This will help ensure overall tax take is not affected.

Case study

Sweden offers reduced VAT on repair services of products such as bikes, footwear and textiles. The Swedish Consumer Association notes this has had a positive effect on uptake of repairs, although some have advocated for a larger reduction than the halving from 25% to 12% that was put in place, to further increase repair incentives. Furthermore, the \$54 million in lost taxes is expected to be more than outweighed by a new tax on harmful chemicals in white goods, demonstrating the synergies with resource use taxes.

Sources: <https://www.weforum.org/agenda/2016/10/sweden-is-tackling-its-throwaway-culture-with-tax-breaks-on-repairs-will-it-work/>

https://lucris.lub.lu.se/ws/portalfiles/portal/77933910/Promoting_the_repair_sector_in_Sweden_2020_IIIEE.pdf

²⁷ <https://committees.parliament.uk/publications/3675/documents/35777/default/> pg.43

²⁸ <https://www.retailgazette.co.uk/blog/2023/10/currys-repair-shop/>

²⁹ <https://www.ihbc.org.uk/resources/VAT-research-FINAL.pdf>

Conclusion

With the Scottish [Circular Economy Bill](#) fully enacted, the Welsh Government's [Circular Economy Strategy](#) nearly four years old and other countries having entrenched incentives, it is essential the UK Government creates a comprehensive roadmap to capture the growth potential of the circular economy. This cannot be achieved without utilising financial incentives to drive business and consumer behaviour. By implementing these policies, the Government can tackle climate change, biodiversity loss and pollution head on, whilst also creating sustainable growth and jobs.

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Annex: other potential financial incentives

Reforming current policies

1. Deposit Return Scheme (DRS)

- **How It Works:** when implemented in 2027, the deposit return scheme will require consumers to pay a small deposit on a product which is refunded when they return the product post-use. It is intended to enable the recovery of cleaner, separated material streams which results in higher quality, higher value secondary materials for onward use.
- **Incentive:** this policy is aimed at shifting consumer behaviour by incentivising them to return items e.g. in the case of DRS for beverage containers, to return empty packaging to reverse vending machines where their deposit will be reimbursed.
- **Additions to current proposals:** given the delays to the introduction of a DRS for beverage containers, the Government has an opportunity to future-proof the scheme by enabling the recovery of refillable beverage containers. Germany's DRS has successfully done this, achieving a 98% return rate and resulting in 42% of all beverages being in refillable containers. Like the German scheme, refillable containers could carry a lower deposit rate than single-use ones.³⁰ Deposit return schemes could also play a vital role in enabling greater uptake of reusable or refillable packaging such as reusable

³⁰ <https://www.tomra.com/en/reverse-vending/media-center/feature-articles/germany-deposit-return-scheme>

food service containers or even bigger ticket items such as electrical products. Being able to recover these valuable resources keeps them in the circular economy for longer.

2. Plastic Packaging Tax (PPT)

- **How It Works:** the PPT was designed to incentivise increased usage of recycled content in plastic packaging, thereby driving down the use of virgin material. Producers are required to pay a levy per tonne of material if their packaging does not contain a minimum of 30% recycled content.
- **Incentive:** this policy aims to incentivise greater use of secondary plastic materials, alongside stimulating investment in the recycling market to service the increased demand arising from the tax.
- **Additions to current proposals:** since its introduction in April 2022, the PPT has raised £553 million for HMRC, exceeding projections.³¹ Producers often suggested it was more affordable to pay the tax than compete for limited recycled material feedstocks. However, HMRC analysis for 2022-2023 shows a downward trend in the tonnages of taxable plastic packaging – indicating the policy is now working. The Government could increase this positive response by setting ambitious recycled content taxes for other materials e.g., paper. To stimulate investment in the domestic recycling market, the tonnage rate could be differentiated between imported recyclate and recyclate which has been manufactured in the UK.

3. Environment Act Single Use Charging Power and Residual Waste Target

- **How It Works:** the Resources and Waste chapter of the Environment Act, 2021 includes the power to introduce charges on single-use items of any material.
- **Incentive:** the Government has yet to fully leverage the Environment Act single-use charging power to drive behaviour change. The plastic bag tax is an example of how a charge has shifted consumer behaviour towards the uptake of reusable bags, driving down use by 98%, delivering against its objectives.³²
- **Additions to current proposals:** single use targets can perversely increase overall material consumption e.g., the charge on plastic bags increased the purchase of 'bags for life', which can contain greater quantities of plastic.³³ Any further single charges should consider how to mitigate this effect. They must be framed within an ambition to reduce the UK's overall material consumption and to reduce burdens on consumers.

³¹ <https://www.gov.uk/government/statistics/plastic-packaging-tax-ppt-statistics/plastic-packaging-tax-ppt-statistics-commentary>

³² <https://www.gov.uk/government/news/plastic-bag-use-falls-by-more-than-98-after-charge-introduction>

³³ <https://www.bbc.co.uk/news/uk-50579077>

Producers should also be required to offer reusable, refillable options as an alternative to single-use.

Driving change in business practices

1. Tax Rebates for Resource Efficiency

- **How It Works:** businesses that meet specific targets, e.g. overall waste reduction, are eligible for tax rebates based on their performance. This would work in a similar way to EPR but could go beyond simply giving companies reduced charges per product sold, to rewarding overall changes in practices, such as changing business models to leasing, rather than selling, reusable products.
- **Incentive:** direct financial compensation for circular practices encourages resource efficiency and reduced waste.
- **Example:** a manufacturing company that can evidence it has reduced resource use by 50% by implementing a leasing scheme receives a reduction in corporation tax or business rates.

2. Changes to Direct Taxation

- **How It Works:** currently, taxes are mainly levied on labour, such as national insurance and income tax, rather than on materials. This incentivises use of virgin materials to create new products, rather than the use of labour to recycle, re-use and repair products. The Government could increase the tax burden on the use of virgin materials and decrease taxation on labour, especially labour focused on the circular economy.
- **Incentive:** in this scenario, businesses that reduce virgin material use would face reduced tax burdens, incentivising resource efficiency, and businesses employing more people to repair products or sell reused products would face less of a tax penalty.
- **Example:** a 30% tax on electricals which are not made with 30% recycled materials from the UK and simultaneously reducing employer national insurance contributions on labour in electronics repair.

3. Green Public Procurement

- **How It Works:** public procurement is worth over £300 billion.³⁴ Governments and local authorities should prioritise awarding contracts to suppliers that demonstrate circular economy practices.

³⁴ <https://commonslibrary.parliament.uk/research-briefings/cbp-9317/>

- **Incentive:** access to government contracts provides a strong financial reason for companies to adopt circular practices. If circular procurement practices were standardised, this would also create a market standard for services and products which aid circular economy goals.
- **Example:** a furniture supplier offering remanufactured or refurbished office furniture is given priority in government procurement contracts.

Encouraging consumer behaviour shifts

1. Zero-Interest Loans or Low-Cost Financing

- **How It Works:** financial institutions, in collaboration with governments, could offer zero-interest loans or low-cost financing to consumers who want to invest in products that reduce resource use and waste, such as home repairs and upgrades.
- **Incentive:** reduces the cost of capital for consumers who want to make investments in products which promote circular use of resources.
- **Example:** households could receive a low-interest loan towards the cost of repairing white goods, such as fridges and washing machines.

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