European Federation for
TRANSPORT and ENVIRONMENT

Making car taxes work for the environment

T&E position paper on the Proposal for a Council Directive on passenger car related taxes' (COM(2005)261 final)

T&E, Brussels, December 2005

Summary of T&E's position

1. T&E strongly *opposes the proposed abolition of the registration tax*;
2. T&E supports the introduction of a *harmonised refund system* to avoid double taxation;
3. T&E favours restructuring BOTH registration and circulation taxes on the basis of CO_2 emissions, but only if the restructuring is done in a way that it indeed *reduces* emissions;
4. T&E urge the Council to widen the scope of CO_2 based taxation as to include taxes on *company cars* and *vans* (light duty vehicles, category N1);
5. T&E favours a deeper and faster change: by 31 December 2008 75% of tax revenue from registration, circulation and company car taxes and taxes on vans should be based on CO_2;
6. Finally, T&E is in favour of aligning CO_2 taxation with CO_2 labelling of passenger cars (and vans obviously), so that there is a perfect and transparent interplay of information and incentives towards consumers.

Background and an explanation of this position follow below.

Background

In July 2005 the European Commission published a long-awaited Proposal for a Council Directive on passenger car related taxes' (COM(2005)261 final, http://europa.eu.int/comm/taxation_customs/taxation/other_taxes/passenger_car/index_en.htm).

The proposal is the last element of the so-called three-pillar strategy to reduce CO_2 emissions from passenger cars, as described in Commission Communication 95/689 and confirmed in the Council Conclusions of 24 June 1996. It has taken almost a decade for this proposal to be finally published.

In brief, The Commission proposes to

- Gradually abolish the registration taxes for passenger cars over a period of five to ten years;
- For the intermediate period until this abolition is complete, to establish a refund scheme to avoid double taxation for people that move from one EU Member State to the other
- Gradually base a part of the annual circulation (and the remaining registration tax) on the CO_2 performance of the vehicle (25% by end 2008, 50% by end 2010)

The proposal will be decided upon in unanimity by the Economic and Financial Affairs Council (the 25 EU Finance or tax ministers), with a consultative role by the European Parliament.

T&E submitted an input to the 2004 consultation on the topic. This position paper elaborates on that submission.

1 Abolition of registration tax: unnecessary and counterproductive

T&E strongly opposes the proposal to abolish passenger car registration taxes for a broad variety of reasons:

- Abolition of the registration tax is very likely to lead to higher emissions and more accidents – and therefore have a negative impact on stated Community objectives in the field of climate change, air quality, road safety and modal split. There are two reasons for this.
    - First, the abolition is very likely to raise car possession and car use. T&E believes that the Commission's assumption that the lost registration taxes will be compensated by increases in other car taxes or fuel taxes – which would reduce emissions and accidents - is not credible. T&E believes that in 'real life' the lost revenue will often be made up through increases (or postponed decreases) of 'bad' taxes such as those on labour or through higher budget deficits.
    - Second, abolition of registration taxes deprives Member States of an excellent tool to promote purchase of more environmentally friendly vehicles. The Netherlands is an example of a country that has frequently used this. In the late 1980s a registration tax break was used to speed up introduction of catalytic converters. On 1 June 2005 a €600 tax break was given to diesel cars with particle filter. And on 1 January 2006 the registration tax was differentiated on the basis of CO_2 performance of the vehicle. Many studies point out that actually differentiation of registration taxes is more effective in influencing consumer choice than differentiation of circulation taxes.
- The key argument to propose abolition of the registration taxes, namely the idea that these taxes impede the functioning of the internal market and therefore harm competitiveness, is badly underpinned. The impact assessment only takes into account the 'ideal' compensation variant in which lost registration tax revenue is made up through higher car circulation or fuel taxes. As already said, in real life it is more likely that the lost revenue will be made up through increases of 'bad' taxes such as those on labour, or through higher budget deficits. The detrimental impacts of such a policy in competitiveness have not been taken into account in the impact assessment.
- Even if the case for harmonisation of car registration taxes were strong, we feel that harmonising them at the average current level in the EU is a better solution than harmonising them at a zero rate. Harmonising them at the average EU level would still give Member States a tool to stimulate sales of cleaner or safer vehicles.
- A secondary argument to abolish the registration tax is to avoid double taxation. We agree that double taxation needs to be addressed, but abolition of car registration taxes is a far too drastic measure to solve this problem. As the Commission itself points out a far lighter solution in the form of a refund system could do this job perfectly.

- Finally, we regret that the expected strong opposition from Finance Ministers against the abolition of the registration tax put the entire proposal at risk, including the welcome element of basing car taxes on CO_2.

2 A refund system: a long-overdue idea to avoid double taxation

As already explained in the previous section, T&E supports the introduction of a system to refund registration taxes refund system to avoid double taxation when citizens decide to register the car in another EU country. Indeed such a move would greatly increase the fairness of taxation and the credibility of the EU project. We believe a harmonised depreciation rate should be agreed and implemented as quickly as possible in order to make the system really work. It should not be the case that people get, for example, 50 per cent of registration taxes back from the state they come from, but still have to pay 60 or 70 per cent in their new home state. Harmonisation is necessary.

3 Base ALL car taxes on CO_2, but only in a way it really works

T&E welcomes in principle the idea of basing car registration and circulation taxes on the CO_2 performance of the vehicle. We would like to add that in our view company car taxes should be included too (see next section), and that there needs to be a guarantee that the new tax system indeed reduces emissions rather than increases them. As an increase might sound paradoxical, we will clarify it.

Currently, most Member States operate circulation taxes on the basis of weight, power or cylinder content of the vehicle concerned. Generally the system is based on the idea that it should be cheap to drive a small car, but that people who can afford a big car are able to pay much more and should hence do so. In other words: the taxes are often stronger than proportionally linked to these vehicle parameters.

One possibility of introducing CO_2 –based taxes is to make them proportional to their CO_2 performance. The table below shows what such a proportional tax would end up like in comparison with the current system for two Opel petrol cars.

Calculation example for the Netherlands: a proportional CO_2 based tax might lead to a bigger cars

Car	Weight (kg)	CO_2 (g/km)	Current tax (€/yr)	Proportional CO_2 based tax* (€/yr)	Tax based on square of (CO_2 minus 80)* (€/yr)
Opel Corsa 1.2	910	146	228	249	174
Opel Omega Station 2.2	1585	236	736	403	973

* Assuming the average tax amount or a petrol car is € 290 (source: CE Delft, The price of transport, 2004) and the average CO_2 emission from a petrol car is 170 g/km.

This example shows that a proportional CO_2 circulation tax would make it more expensive to drive the – low CO_2 - Opel Corsa and make it cheaper to drive the – high CO_2 - Opel Omega. Such a system hence makes it more attractive to own big cars than the current tax system. This example raises at least the question whether the environmental outcome of such a change in taxation is positive.

It also shows that a CO_2 tax that is much stronger than proportional – for example based on the square of the CO_2 emissions per km minus 80 – could have the reverse impact: it could make it more attractive to own the Corsa than the Omega.

Concluding, Member States should in our view demonstrate that their changes in circulation taxes are indeed environmentally beneficial and do not have perverse effects such as those pointed out above.

4 Broaden scope of CO_2 taxation to cover taxes on *company cars and vans*

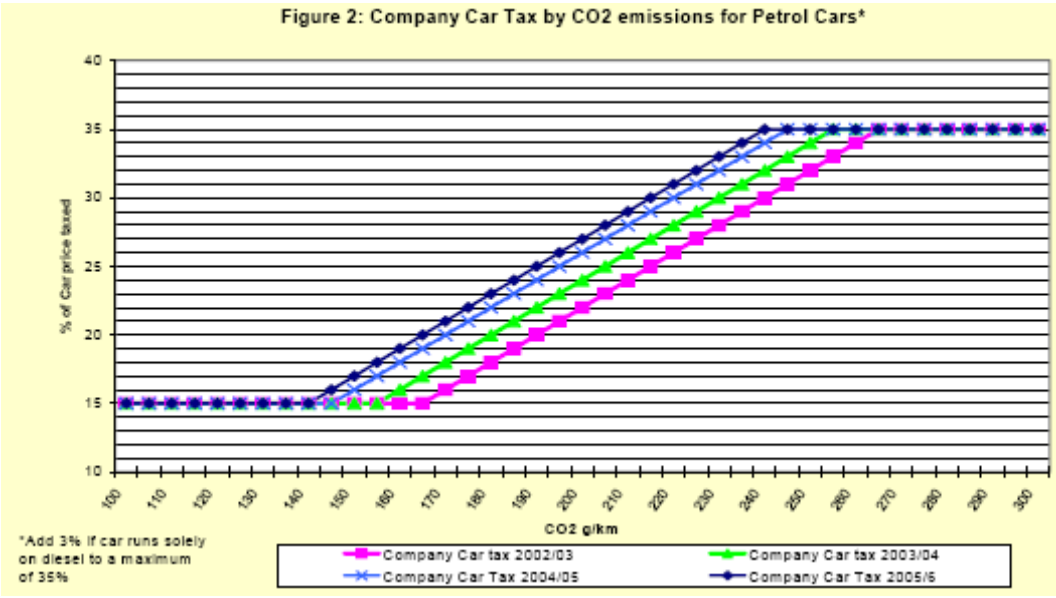
Inclusion of company car taxes

In many member stats company cars make up to 50 per cent of new car sales. In addition, many company car fuel bills are not paid by the employee. Therefore, incentives to influence the purchase and driving decisions of company car drivers towards lower CO_2 are currently largely absent and should be introduced as quickly as possible.

This Directive offers such an opportunity. Linking national company car taxation systems to the CO_2 performance would be a good way of introducing such an incentive. All EU Member States oblige employees to add an amount to their income when they drive a car that is owned and paid for by the company they work for. The employee in turn pays a higher income tax. The reasoning for this arrangement is that such a car constitutes a form of salary. Generally this addition to the taxable income is related to the car price.

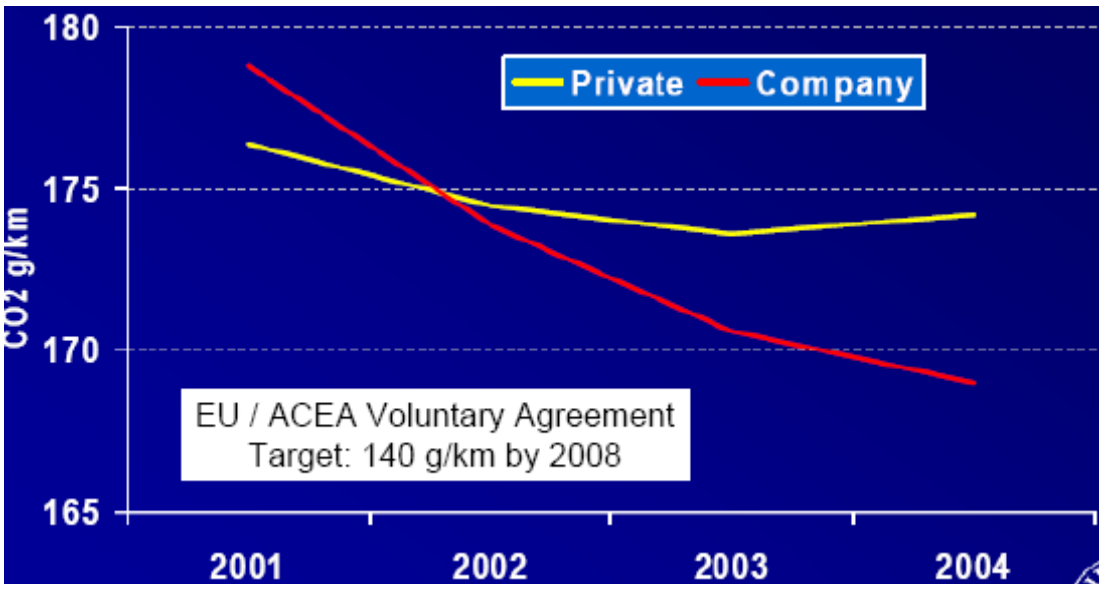
The UK is the only country that has based the percentage of the car price to be added on the CO_2 performance of the car.

Graph: The percentage of the company car price added to the taxed income as a function of the car's CO_2 emission in the UK



The impact of the scheme is substantial – between 1999 (when the scheme was announced) and 2004 average CO_2 emissions from company cars dropped from 196 to 169 g/km or 14 per cent, which is double the rate of improvement of the EU as a whole over that period. In 2002, company cars were for the first time more fuel efficient than private cars. See the graph below

The development of CO_2 emissions (g/km) for new private and company cars in the UK (presentation Energy Saving Trust on CARS21 public hearing, http://europa.eu.int/comm/enterprise/automotive/pagesbackground/competitiveness/cars21_hearing/est.pdf)



In addition, the *Report on the evaluation of the Company Car Tax Reform* (April 2004, http://www.hmrc.gov.uk/cars/cct_eval_rep.pdf) showed that the programme (started in April 2002) was on track to achieve its target of 1.5 to 3 per cent reduction of CO_2 emissions from road transport in the UK.

Inclusion of vans

Vans (often called light duty commercial vehicles, or N1 vehicles) are also important in CO_2 terms. Based on a recent TNO study (*Measuring and preparing reduction measures for CO_2 emissions from N1 vehicles*, November 2004) it can be estimated that vans in the EU25 currently emit approximately 100 MT of CO_2, which is about one sixth of passenger car CO_2 emissions.

Directive 2004/3 regulates measurement of CO_2 emissions from new vans. Emissions from new light vans (under 1,305 kg) have to be measured as of 2005, and those of heavier vans have to measured as of 2007.

This implies that inclusion of vans in the CO_2 taxation has become an open possibility, and a possibility that is not included in the Commission proposal, probably because of the very long drafting process.

It is therefore not more than logical to extend to scope of the CO_2 based car taxes to the state-of-the-art, i.e. cars AND vans.

5 Go for 75% CO_2 based taxation by 31 December 2008

The Commission proposes that by 31 December 2008 at least 25% of the annual circulation tax should be based on CO_2, and that two years later the minimum percentage should increase to 50 per cent. We favour a deeper and faster transformation of the tax base. The implementation difficulty is more related to the change of the tax base than to the percentage of tax that should be based on CO_2 Therefore, we do not see the why a gradual implementation is necessary and favour

75% of car taxes based on CO_2 as of 31 December 2008. The other 25% can be used to stimulate cars with a better air pollution performance (Euro classes) or cars equipped with certain safety features such as alcohol locks.

As already said, the percentages should not just apply to annual car circulation taxes, but also to registration taxes, company car taxes, and to taxes on vans.

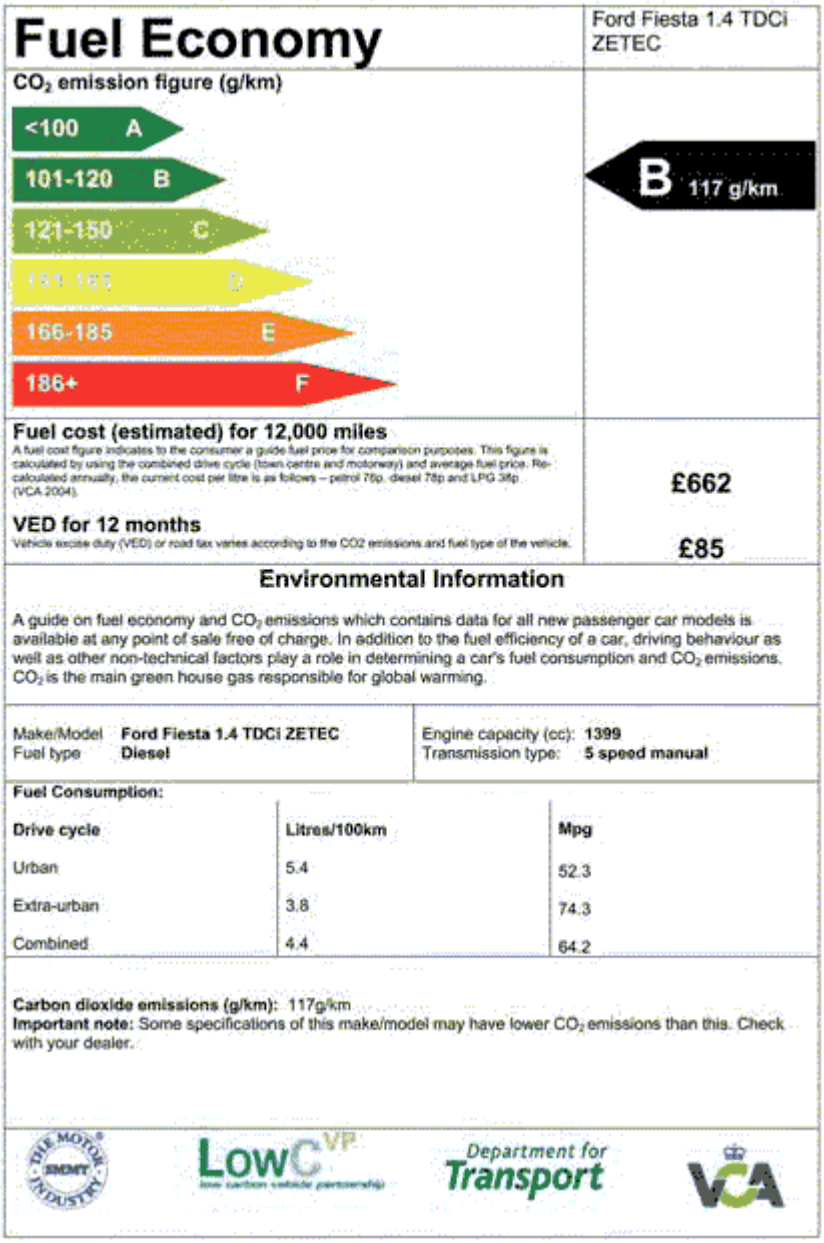
6 Align fiscal incentives with consumer information

Finally, it is very important to give consistent signals to consumers. The EU Labelling Directive 1999/94 stipulates provision of CO_2 information in car showrooms, special booklets and car advertisements. But the Directive leaves a wide scope for national implementation and the result is a myriad of different labels, forms et cetera over the 25 EU Member States. Only a few countries operate colour-code schemes such as those for fridges and washing machines, and only very few provide information on annual fuel costs.

The combination of information on CO_2 emissions and fuel costs with fiscal incentives offers a great opportunity to raise awareness amongst consumers of the environmental and financial impact of their car choice. Linking fiscal incentives with colour codes for CO_2 emissions seems the most transparent and recognisable way forward.

Just as in case of company cars, the UK is ‘best practice’. It has a colour-coded CO_2 label. The label mentions annual fuel costs, to link the CO_2 figure to the customer’s purse. And the colours are linked to the annual vehicle circulation tax (VED, Vehicle Excise Duty). The weak point of the system is that the differences in VED levels are too small (around €145 per year difference between a high or low CO_2 car) to have a significant impact on consumer choice.

The UK's colour-coded fuel economy label, annual fuel cost indication and the link with the VED, Vehicle Excise Duty, the UK's annual vehicle circulation tax.



Fuel Economy

Ford Fiesta 1.4 TDCi ZETEC

CO_2 emission figure (g/km)

<100 A
101-120 B
121-150 C
151-165 D
166-185 E
186+ F

B 117 g/km

Fuel cost (estimated) for 12,000 miles

A fuel cost figure indicates to the consumer a guide fuel price for comparison purposes. This figure is calculated by using the combined drive cycle (town centre and motorway) and average fuel price. Re-calculated annually, the current cost per litre is as follows – petrol 76p, diesel 78p and LPG 38p (VCA 2004).

£662

VED for 12 months

Vehicle excise duty (VED) or road tax varies according to the CO2 emissions and fuel type of the vehicle.

£85

Environmental Information

A guide on fuel economy and CO_2 emissions which contains data for all new passenger car models is available at any point of sale free of charge. In addition to the fuel efficiency of a car, driving behaviour as well as other non-technical factors play a role in determining a car's fuel consumption and CO_2 emissions. CO_2 is the main green house gas responsible for global warming.

Make/Model **Ford Fiesta 1.4 TDCi ZETEC**
Fuel type **Diesel**
Engine capacity (cc): **1399**
Transmission type: **5 speed manual**

Fuel Consumption:

Drive cycle	Litres/100km	Mpg
Urban	5.4	52.3
Extra-urban	3.8	74.3
Combined	4.4	64.2

Carbon dioxide emissions (g/km): 117g/km
Important note: Some specifications of this make/model may have lower CO_2 emissions than this. Check with your dealer.

For further information:

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