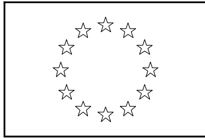


COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 06.09.2002
COM(2002) 431 final

COMMUNICATION FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN PARLIAMENT

TAXATION OF PASSENGERS CARS IN THE EUROPEAN UNION - options for action at national and Community levels

{SEC(2002)858}

TABLE OF CONTENTS

1. Introduction ... 3
2. Passenger Car related taxes - Current state of play ... 5
2.1. Impact on national budgets ... 5
2.2. Registration Tax (RT): ... 6
2.3. Annual Circulation Tax (ACT) ... 6
2.4. Value Added Tax (VAT) ... 7
2.5. Fuel taxes (FT) ... 7
3. Passenger car Taxation, the internal market and current community law ... 8
3.1. Impact on the Internal Market and the EU-citizen ... 8
3.2. Current state of Community law with regard to vehicle taxation ... 10
3.2.1. Existing Community legislation ... 10
3.2.2. Identification of the main problems raised by citizens and car trade ... 11
4. Removing tax obstacles in the internal market for passenger cars: a new approach to passenger car taxation ... 14
5. Passenger car taxation as one of the tools to reduce CO_2 emissions from new passenger cars ... 16
5.1. Introduction ... 16
5.2. Fiscal measures, a tool for CO_2 emissions reduction ... 18
5.3. Tax differentiation based on CO_2 sensitive parameters ... 18
5.4. Company car taxation ... 20
6. Conclusions and Policy Recommendations ... 22
Annex: Tables and figures from the TIS and the COWI studies {SEC(2002)858}

1. INTRODUCTION

Motoring has been an important source of revenue for a long time. All Member States rely heavily on a range of tax instruments to ensure significant budgetary receipts from both private and commercial road users. The vehicle related taxation systems implemented in the Member States reflect a variety of influences beyond the obvious need to raise revenue: geographic, industrial, social, environmental, energy and transport policy considerations can all have a bearing on the type of approach followed.

The variety of influences has led, traditionally, to large differences in the overall strategies followed in the Member States. These differences apply both in terms of the overall level of dependence on the sector for a contribution to total revenues, the choice of instruments and their precise implementation. The operation of 15 different vehicle tax systems within the EU has resulted in tax obstacles, distortions and inefficiencies. From an *internal market* point of view the car market in the EU is still a long way from a true single market.

- From the *citizen*'s viewpoint, the notion of a single market implies freedom to move between Member States and buy a car in the Member State of his choice, and to pay purchase-related taxes in that State. The citizen expected that the levels of vehicle taxes would be approximated and that problems associated with movement - either temporary or permanent - between Member States would disappear. The citizen is often asked to pay a Registration Tax (RT) twice, if he moves his passenger car from one Member State to another, both of which apply a RT.

- From the *motor industry* viewpoint, the wide differences in tax systems have a negative impact on their ability to achieve the potential benefits of operating within a single market, and consequently to improve competitiveness and create new jobs. On the other hand, precisely because of the differences in tax levels, the car industry adapts its pre-tax prices taking into consideration the level of taxation in Member States. Pre-tax prices are much higher in those Member States applying no, or a low, RT.

From an *environmental* point of view, it should be recalled that transport is responsible for 28% of total CO_2 emissions. Road transport alone currently represents 84% of all transport related CO_2 emissions; more than half is accounted for by passenger cars[1].

The Gothenburg European Council, in June 2001, confirmed that combating climate change is a major priority of the European Union's Sustainable Development Strategy. In March 2002 the Council ratified the Kyoto Protocol on behalf of the European Community. This shows the urgency of a successful implementation of the *Community's strategy to reduce CO_2 emissions from passenger cars and improve fuel economy*. The use of fiscal measures is one of the pillars of this strategy.

---

[1] Passenger car means the category M1 as defined in Annex I of Council Directive 70/156/EEC (OJ L 42 of 23.2.1970, p. 1-15).

In the Communication on "*Tax policy in the European Union - Priorities for the years ahead*" [2], the Commission sets out its views on the fundamental priorities for tax policy in the European Union in the years ahead. It must serve the interests and wishes of citizens and business to benefit fully from the internal market. This means that it is necessary to focus on the removal of tax obstacles and distortions, the elimination of inefficiencies linked to the operation of 15 different tax systems within the EU, and the simplification of these tax systems to make them more accessible to citizens. EU tax policy must also reinforce, inter alia, EU sustainable development, environmental and energy policies. In the view of the Commission, vehicle taxation is an area where this new tax policy approach should be applied. The Commission considers it useful to have a debate on these important issues. This Communication can serve as a starting point for this debate.

Objective of the Communication

The main purpose of this Communication is to propose, for discussion in the Council and the European Parliament, policies and options for future action in the field of passenger car taxation.

The priority is to ensure the smooth functioning of the Internal Market and, at the same time, to advance other policy objectives, in particular the Community's environmental objectives provided for by the Kyoto Protocol.

The Communication is based on the outcome of two recent studies, as well as a number of best practices in use by Member States. It explores possibilities to:

- modernise and simplify the existing vehicle taxation systems, and in particular to include new parameters in the tax bases of passenger car related taxes, in order to make them partially, or totally, CO_2 based;

- better co-ordinate and, at a later stage, to approximate passenger car taxation systems, and to remove tax obstacles and distortions to free circulation of passenger cars within the Internal Market.

[2] COM(2001)260 final (OJ C284 of 10.10.2001, p. 6-19)

2. PASSENGER CAR RELATED TAXES - CURRENT STATE OF PLAY

Taxes on passenger cars are very diversified in terms of structure and levels. They are based on one or a mix of elements such as fiscal horsepower, engine capacity, weight, kW, price of the car, fuel consumption, or CO_2 emissions. Tables 1, 3, 5 and 6 in Annex, give a clearer picture of these taxes.

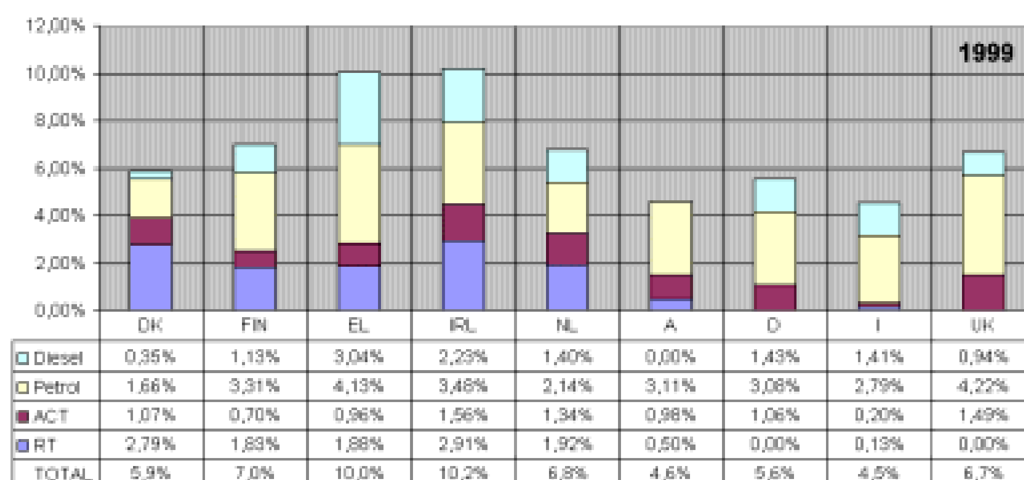
Taxes and charges on passenger cars include:

- taxes payable at the time of acquisition, or first putting into service, of a passenger car, defined in most cases as Registration Tax (RT);
- periodic taxes payable in connection with the ownership of the passenger car, defined in most cases as Annual Circulation Tax (ACT);
- taxes on fuel (FT);
- any other taxes and charges, such as insurance taxes, registration fees, road user charges, road tolls etc.

This Communication focuses on RT, ACT and to some extent fuel taxes, as they are by far the most important passenger car related taxes.

2.1. Impact on national budgets

The level of budgetary dependence on vehicle related taxes varies considerably from one Member State to another. The following Figure, and Table 8 in Annex, present this dependence, in absolute and relative terms, in nine Member States:



	DK	FIN	EL	IRL	NL	A	D	I	UK
Diesel	0,35%	1,13%	3,04%	2,23%	1,40%	0,00%	1,43%	1,41%	0,94%
Petrol	1,66%	3,31%	4,13%	3,48%	2,14%	3,11%	3,08%	2,79%	4,22%
ACT	1,07%	0,70%	0,96%	1,56%	1,34%	0,98%	1,06%	0,20%	1,49%
RT	2,79%	1,83%	1,88%	2,91%	1,92%	0,50%	0,00%	0,13%	0,00%
TOTAL	5,9%	7,0%	10,0%	10,2%	6,8%	4,6%	5,6%	4,5%	6,7%

Figure1: Revenue from vehicle related taxes as % of total taxation, in 1999
Source: TIS study[3], Figure 26. For Austria petrol figures also include diesel figures.

---

[3] Study on vehicle taxation in the Member States of the EU, January 2002, TIS/PT. The study covered a representative number of high, medium and low taxing Member States and is available under the following web site address: http://europa.eu.int/comm/taxation_customs/taxation/car_taxes/vehicle_tax_study_15-02-2002.pdf

2.2. Registration Tax (RT):

- Ten Member States are currently applying a RT[4].
- Tax bases and tax levels currently applied are strongly diversified; tax levels range, in extreme cases, between zero and 180% of pre-tax car price. In absolute terms average RT ranged, in 1999, between 15659 EUR in Denmark and 267 EUR in Italy.
- RT concerns most of the complaints European citizens rise, contesting in particular, disproportionate rates, or double payment of RT. In case of exportation of a passenger car, or its permanent removal to another Member State, the absence of a RT refund system makes partial recovery of RT impossible.
- The significant differences in RT levels partly influence the pre-tax price of passenger cars, and provide an incentive to citizens to purchase their vehicles in a Member State with high RT, since the pre-tax prices in these Member States are, as a rule, lower.

Member States having a large car industry tend not to apply a RT, or they apply a lower RT, while car importing Member States tend to levy higher RT. In 1999, relatively high average RT levels were found, for example, in DK, FIN and NL, while five Member States did not apply a RT. As shown in table 5, most tax bases are based on sale prices, although rates may be differentiated according to cm³.

2.3. Annual Circulation Tax (ACT)

All Member States apart from France apply ACT at national level. Very different objective factors are used as tax bases (e.g. cm³, kW, CO_2, weight), which are often further adjusted at national level to define country-specific fiscal parameters and brackets (e.g. fiscal horsepower based on cm³) or environmental objectives (e.g. differentiation in accordance to compliance with emission limits (EURO II, III and IV). As far as effective rates are concerned, high average levels of ACT were found, for example, in DK, NL and IRL. In most Member States, diesel cars face higher ACT than petrol cars of the same size, mainly in order to compensate for the lower diesel fuel taxes.

- Fourteen Member States[5] are currently applying an ACT.
- Tax bases used and tax levels applied are very diversified; the average ACT paid in 1999 ranged from 30 EUR/vehicle in Italy, to 463 EUR/vehicle in Denmark.
- ACT has the advantage of being a more stable source of revenue (less sensitive to economic cycles) than RT, since ACT produces its revenue during the entire lifetime of a vehicle, unlike RT, which produces its revenue upon purchase of a passenger car.
- Important differences in average ACT levels can provide an incentive to citizens to register their passenger car in a Member State other than the Member State where they have their permanent residence.

[4] D, F, L, S and UK do not apply any RT.

[5] In 2000 F has abolished ACT for passenger cars used by private persons.

2.4. Value Added Tax (VAT)

VAT is subject to a Community-wide regime, which imposes, in the case of new cars, a considerable degree of common rules. Motor vehicles are generally subjected to the standard rate of VAT (see Table 1, in Annex). Common rules govern the method of calculation of the taxable amount.

After the completion of the Internal Market in 1993, Member States, which had previously applied a luxury VAT rate and/or an excise duty on cars, adapted their vehicle tax systems, replacing these taxes with registration taxes. Furthermore, it became clear that, given the existing differences in VAT rates, Member States wanted VAT on all means of transport to be collected in the jurisdiction, and at the rate of the country where the owner of the vehicle resides. Generally, a non-taxable person is allowed to purchase goods within the Community and pay the VAT in the Member States where the goods are purchased. However, since the introduction of the transitional VAT arrangements, this principle has been adjusted for the purchase of new means of transport. In this case VAT is due in the Member State of destination, which normally coincides with the country where the vehicle is registered. This situation, which contrasts with the general rules applicable to other consumer goods purchased in the internal market and which does not favour convergence of the VAT scheme applied to passenger cars, is the result of non-approximation of VAT rates.

2.5. Fuel taxes (FT)

Excise duties on motor fuels are seen as an effective fiscal instrument to collect revenue, to influence the level of car use, or for internalising environmental and social costs linked to the use of passenger cars, such as infrastructure costs, accident costs, and air pollution costs. Given the direct relation between CO_2 emission and fuel consumption they are a particularly effective instrument to internalise the external cost of emissions. Usually, Member States applying no, or low RT, compensate revenue losses by higher fuel tax levels. With the only exception of the UK, they all apply lower tax levels on diesel, traditionally used by commercial vehicles. Diesel is taxed on average about 140 EUR/1000 litres lower than unleaded petrol.

This difference in taxation on diesel would no longer be justifiable if taxation on diesel used as fuel for commercial uses, was de-coupled from taxation of diesel for private use. The Commission has already supported the view that the excise duty on diesel, used as fuel for private cars, should be gradually aligned to the excise duty imposed on unleaded petrol (see Proposal for a Council Directive COM (2002) 410 final). Indeed, such approximation would reduce tax distortions and be environmentally consistent. Despite a more positive balance than petrol as far as CO_2 emissions are concerned, the combustion of diesel fuel in today's passenger cars' engines triggers other environmental problems (e.g. particulate matters, nitrogen dioxide). However, it can be expected that these differences between diesel and petrol engines used in passenger cars will disappear within the coming years. Taking into account all these aspects, there is no a-priori justification from an environmental viewpoint to tax the two types of fuel differently.

3. PASSENGER CAR TAXATION, THE INTERNAL MARKET AND CURRENT COMMUNITY LAW

3.1. Impact on the Internal Market and the EU-citizen

The great variety in vehicle taxation systems, their tax bases and rates, has a significant impact on the Internal Market.

Important differences in pre-tax car prices

As vehicle taxes are paid in the Member State where the vehicle is to be used, pre-tax car price could be an important factor likely to influence cross-border trade. The car industry establishes recommended pre-tax prices, which consumers should pay for a particular car model, taking into account, among other factors, consumer purchasing power, and the level of taxation in each Member State. These prices are in general higher in Member States applying no, or low, RT. Since cross-border retailing and purchases in the Internal market do not take place to any significant extent, in response to high RT in some MS, car manufacturers fix pre-tax prices at a lower level than in MS applying no, or low, RT (see Table 4 in Annex for a synthesis[6]). Different taxation levels can explain about 20% of the European car price differentials[7].

Car market fragmentation

The wide differences in tax systems have a negative impact on the ability of the car industry and European consumers to reap the benefits of operating within a single market. Car market fragmentation prevents industry from exploiting economies of scale, or to produce motor vehicles for the entire Internal Market, applying the same specifications and does not prevent pre-tax prices from varying significantly within the internal market. Industry is often obliged to produce a specific car model, with different specifications, in order to soften the pre-tax prices, in particular when the vehicle is destined to high taxing Member States. This generates additional costs that undermine the competitiveness of the European car industry, and consequently, has negative repercussions on the employment situation in the EU. In parallel, as tax requirements differ, cars marketed in one Member State with specifications designed to meet national requirements and "tax influenced" demand (e.g. brackets of fiscal horsepower, tax policy regarding diesel), are imperfect substitutes of and may not effectively compete with cars sold in a different Member State, thereby undermining the benefits which EU consumers should derive from a competitive and integrated market.

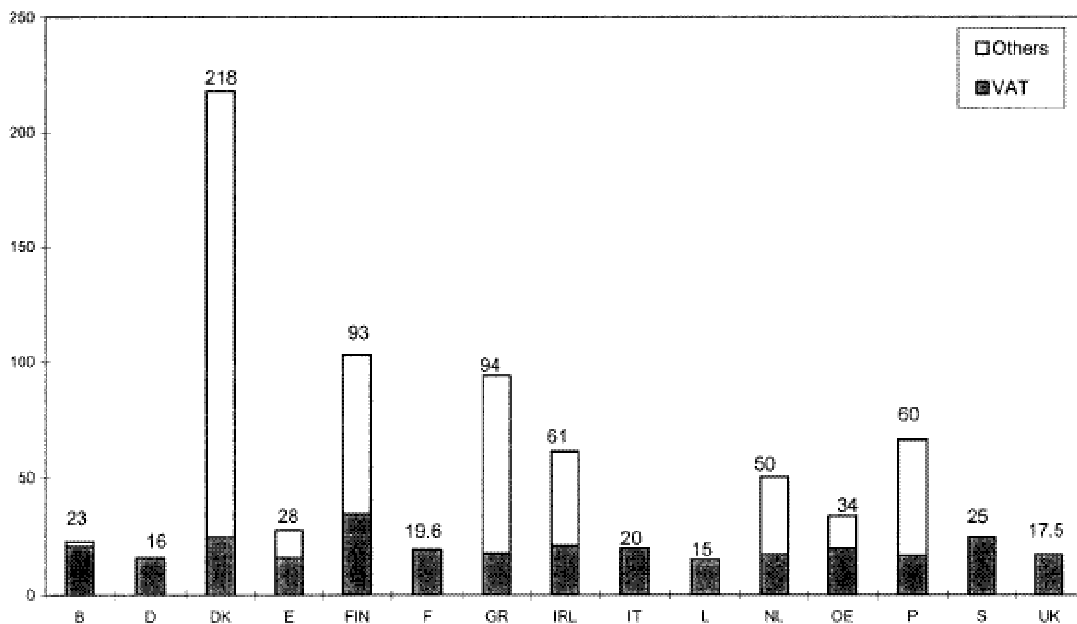
Figure 2 hereafter, presenting tax as % of the pre-tax price of the car, provides an example of how RT and VAT are affecting retail prices of a 2000 cc passenger vehicle in all EU Member States:

---

[6] Comprehensive information about price differentials, pre and post tax prices in the EU is available in the biannual report on car prices, which can be found in: http://europa.eu.int/comm/competition/car_sector/price_diffs/. See also Press release IP/02/305 of 25.2.2002.

[7] See TIS study

Car capacity: 2000 cc



Source: ACEA Guide, updated in April 2001

Tax consequences of cross border transfers of cars

Cars are important means of transport for their users, and assist them to exercise the right of free circulation granted by the EC Treaty. Many citizens take their car when they move, either temporarily or permanently, from one Member State to another. Other citizens buy, or hire, a car in another Member State.

For the EU-citizen, many questions arise with regard to the fiscal consequences of these cross border transfers of cars. When a car is moved from a Member State to another, different tax structures and administrative problems lead to a lack of transparency, and increase transaction costs for the consumer.

Although ACT is sometimes reimbursed, RT is never re-paid when a car is transferred to another Member State. Member States that levy RT require that a RT has to be paid (again), when a car is to remain permanently on their territory. Double taxation and other fiscal consequences of cross border transfers of cars are dealt with in section 3.2.

Other barriers to cross border transfers of cars

Apart from the fact that the citizen can be confronted with double taxation, the procedure necessary for moving a car from one Member State to another is often very complex. There is a lack of comprehensive and easily accessible information on this issue for the EU citizen. Although taxation is not the only reason for this procedure, the significant difference in car taxation levels between Member States is one of the main reasons for it. From the citizen's viewpoint, these complex procedures act as evidence that we are a long way from a true single market.

The following list provides some quantified information concerning certain additional costs that the EU citizen has to face:

- In case of exportation[8] of a vehicle, workload for the citizen for de-registration ranges between few minutes and one day. It requires the presentation of between 5-11 documents, and to contact a number of institutions ranging between 1-5. Total cost, involving de-registration fee, temporary road permit, and other costs, can range between zero and 64 EUR.
- In case of importation of a vehicle, workload for the citizen for registration ranges between one and nine hours. It requires the presentation of between 1-9 documents, and to contact a number of institutions ranging between 1-7. The total cost, involving registration fee[9], temporary road permits, other costs, is much higher, and can range between 70 and 437 EUR.
- The average cost for the citizen, who moves his place of residence to another Member State, and takes his car with him, is estimated to be up to 351 EUR.
- Information on vehicle exportation is, with the exception of NL, available only in national language; on importation, only in DK, NL and IRL is a certain amount of information available in a foreign language.
- The assistance of a native speaker, or even a specialist is often necessary for a private EU citizen, to accomplish the cross border transfer procedures, particularly if some documents must be completed in the national language.

3.2. Current state of Community law with regard to vehicle taxation

The way Member States apply their car taxes gives rise to an increasing number of complaints by citizens and the car trade to the European Commission, petitions to the European Parliament, and cases before the Court of Justice.

The Commission has made an analysis of current Community law and of the jurisprudence of the Court of Justice. This analysis is laid down in a Working paper of the Commission, which indicates the rights that citizens have at present when moving (with) their cars from one Member State to another Member State. This Working paper is provided at the following Internet addresses: http://citizens.eu.int/originchoice.htm or http://europa.eu.int/citizens.

3.2.1. Existing Community legislation

Two Council Directives[10] were introduced in 1983 concerning the tax treatment of private vehicles when persons move, either temporarily or permanently, from one Member State to another. At that time, fiscal frontiers between Member States still existed. In 1998, the Commission put forward a proposal[11] to replace these two Directives by a new one, to update the existing Community legislation in this area, and to better address the situations that arise with greater freedom of movement under an internal market. So far, this proposal has failed to secure agreement at Council.

[8] For the purpose of this analysis the terms exportation and importation cover both importations from and exportations to third countries as well as vehicle transfers to and from another EU Member States.

[9] Registration fee is a separate charge and should not be confused with RT (Table 1 in Annex)

[10] Directives 83/182/EEC and 83/183/EEC (OJ L 105 of 23.4.1983, p. 59-67)

[11] COM(98)30 final (OJ C108 of 7.4.1998, p. 75-81)

Furthermore, the Commission observes that if passenger cars are transferred, "imported", from one Member State to another, Member States have to respect the general principles of the EC Treaty and shall not:

– give rise to border-crossing formalities in trade between Member States (Article 3 (3) of Directive 92/12/EEC);

– impose charges having equivalent effect to Customs duties (Article 23 and 25 of the EC Treaty);

– impose internal taxation of any kind in excess of that imposed on similar domestic products (Article 90 of the EC Treaty).

Over recent years, the EC Treaty itself has undergone some important changes. Article 14 states that, the internal market shall comprise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of this Treaty. On the basis of Article 18 of the Treaty, every citizen of the Union shall have the right to move and reside freely within the territory of the Member States. An indirect attack on this freedom by means of an unjustified tax on vehicles, which are the means most used to exercise this free movement, is not acceptable.

The two above-mentioned Directives, as well as Article 90 of the EC Treaty, have already led to an abundant case law of the Court of Justice, which has specified, and limited, the competence of the Member States to tax cars transferred from one Member State to another.

3.2.2. *Identification of the main problems raised by citizens and car trade*

Based on the analysis made in the above-mentioned Working Paper of the Commission, this section shows what are the main issues:

a) RT on definitive transfer of a vehicle to another Member State (without change of residence of the owner)

A definitive transfer normally implies that new registration (standard plates) will be necessary in the Member State of destination.

Currently, certain taxes other than VAT (in particular RT) can be required to be paid at this time in the Member State of destination, even if comparable taxes have already been paid in the Member State of origin. However, the above-mentioned provisions of Community law limit the taxing powers of the Member States in this field (see the Commission's Working paper on the Internet site).

The main complaint with regard to such transfer relates to the excessive residual values for second hand cars that are applied by the Member State of destination, which result in high, and disproportionate, RT amounts. These amounts of RT applied on "imported" cars, were found in a number of cases to be higher than the residual RT amounts corresponding to similar cars circulating on the same national markets. The Court has already identified a number of objective criteria with regard to the determination of the residual value, which include the vehicle's age, make or

model, mileage, method of propulsion, general condition, the mechanical state or the state of maintenance of the vehicle[12]. Member States are obliged to apply a transparent method for calculating the residual value of second hand passenger cars, and to enforce the application of these objective criteria established by the Court of Justice. However, some of these criteria can be difficult to apply in practice.

b) Disproportionate level of registration fees in the case of transfers of vehicles in the event of change of normal residence

If the transfer of the vehicle coincides with the change of normal residence, the citizen is normally not obliged to pay again a tax, like the RT, in the Member State of his new residence. However, in order to benefit from the exemption, a number of conditions must generally be fulfilled, which are stipulated by Directive 83/183/EEC. The only taxes for which the citizen will become liable in the Member State of his new residence, as from the moment he begins to use the vehicle in this Member State, are periodic taxes (monthly or annual) connected with the use of the vehicle within the Member State, generally called ACT.

It must be observed, however, that the Member State of the new residence can charge certain “fees” at the time of registration of the vehicle, the amount of which should be limited to the approximate cost of the services rendered (registration fees). These fees should not to be confused with the RT, or similar taxes. As Member States can make a confusion between "registration fees" and "registration taxes", citizens are sometimes invited to pay duties in some Member States which seem disproportionate to be considered as a fee.

c) The absence of a (partial) refund of the RT paid in the Member State of first registration

The absence of a refund system, which would allow for partial reimbursement of the RT paid in the Member State of first registration, appears to be a major concern for citizens and the car trade.

Discussions on the possible non-conformity with Community law of a refusal of a Member State to reimburse (partially) the RT paid in that State, can be expected to be influenced by the forthcoming case law of the Court of Justice (see the Commission’s Working paper on the Internet site).

d) Place of normal residence and registration of the vehicle

Normally, the place of establishment of the vehicle coincides with the Member State of the citizen's normal residence. In this Member State the vehicle must be registered, use the standard plates, and is subject to the vehicle related taxes, particularly RT and ACT. However, in exceptional cases, a person may want to register a passenger car in a Member State other than that of his normal residence – or may reasonably be invited to do so by the authorities of that other Member State - (e.g. in the Member State of his second residence), if he returns very often to that Member State, and for reasons linked to distance he is unable to use his vehicle registered in the Member State of normal residence. Such a situation must not give rise to a double taxation (see the Commission’s Working paper on the Internet site).

---

[12] ECJ, 22 February 2001, C-393/98 Gomes Valente Rec. p I-1327, points 24, 26, and 28

On the basis of the analysis in this Chapter the Commission is of the opinion that:

- the way car taxes, in particular RT, are still applied by (some) Member States amounts to a clear obstacle to the freedom of movement in the Internal Market;
- although existing Community legislation, and the case law of the Court of Justice, help to resolve a number of problems that the European citizens face, new legislation would increase legal certainty, and reduce the number of complaints by citizens;
- Community legislation, governing the treatment of vehicles moving between Member States, should therefore be adapted, in order to achieve a more efficient Internal Market without internal tax obstacles.

4. REMOVING TAX OBSTACLES IN THE INTERNAL MARKET FOR PASSENGER CARS: A NEW APPROACH TO PASSENGER CAR TAXATION

Gradual reduction of Registration Tax

In the opinion of the Commission there is a valid reason for a gradual reduction of RT divergences in the EU.

A gradual transfer of revenue should take place from RT to ACT and to some extent, to fuel tax. This should lead to a RT stabilisation at low levels, or preferably, to a complete abolition of RT in the long term. Such a transfer would:

- provide more fiscal stability for the budget. ACT is a more stable source of revenue than RT. Revenues of RT are dependent on yearly car sales, which can show quite strong fluctuations
- provide for car consumer price approximation in the EU
- result in more vehicle tax approximation in the EU
- bring forward in some MS significant retail car price reductions
- require a transitional period, in order to avoid an excessive tax burden on those who have bought a new car and paid a high RT, and also having to pay a higher ACT
- improve the functioning of the Internal Market and the competitiveness of the European car industry, for the benefit of the European citizen
- cause transition costs in the Member States with a (very) high RT. These structural changes in vehicle taxation seem feasible however, taking into account the establishment of a sufficiently long transitional period.

Because the above-mentioned shift from RT to ACT and fuel tax, requires a rather long transitional period, **additional legal measures** are appropriate to deal with the problems which citizens and the car trade face today, and to offer them simple and uniformly applicable rules.

Therefore, the Commission intends to propose the following measures, which go beyond what was foreseen in the 1998 proposal for a Directive:

- general rules with regard to the **method of calculation of the RT** on used cars imported from other Member States. The jurisprudence of the Court of Justice (in particular the Gomes Valente case, C-393/98) contains important interpretations that could be translated in harmonised Community rules. This would result in more legal certainty and transparency for the citizen;

- **a refund system for the RT** in cases where a used car is sold to another MS or exported to a third country. The way of calculating the residual RT to refund should be the same as in the case of import of used cars from other Member States;

- when ACT has previously been paid for a number of months following the removal of a vehicle to another Member State, **double taxation of ACT** must be avoided. This implies that Member States would have to grant a refund of the ACT already paid for the number of months following the removal of the vehicle from their territory

Refund system for Registration Tax

In the view of the Commission a harmonised RT refund system should be established without delay in all ten Member States currently applying a RT. This refund should apply to used cars, which are transferred permanently to another Member State (by a EU citizen, or by a car trade company). Clear rules on such a system would be helpful to the citizen. It would also have a positive influence on the export of used cars, because prices can be lower as a consequence of the refund of RT.

The refund system should also apply in the case of cars moved permanently to another Member State in connection with a transfer of residence. For these cases the 1983 Directive - and the 1998 proposal for a Directive - provide for the application of an exemption of RT in the Member State of arrival. If such an exemption is granted, there is no need for a refund of the RT in the Member State of departure, because the citizen is not faced with double taxation[13]. The Commission considers that it would be more clear and simple to apply a refund system in all cases where a used car is transferred permanently to another Member State (i.e. in connection to transfer of residence, and in cases where a used car is sold to another Member State).

Taking into account the above-mentioned amendments, the Commission considers it is to be preferred to withdraw its 1998 proposal and replace it by a new proposal incorporating all new elements referred to in this Chapter.

[13] See article 2 (2) (a) of Directive 83/183/EEC and article 4 (1) (a) of the proposal for a Directive COM(98)30 final. An exemption is only granted if the car was not subject to an exemption or refund in the MS from which it is brought.

5. PASSENGER CAR TAXATION AS ONE OF THE TOOLS TO REDUCE CO_2 EMISSIONS FROM NEW PASSENGER CARS

5.1. Introduction

In order to reduce CO_2 emissions the Council endorsed in 1996[14] the Community strategy to reduce CO_2 emissions from passenger cars and improve fuel economy[15], which is based on three pillars[16]:

- Commitments of the car industry on fuel economy improvements[17].
- Fuel-economy labelling[18]
- Fiscal measures

The European Council and the European Parliament have adopted a target of reducing CO_2 emissions from new passenger cars to 120 gram per kilometre by 2005, or by 2010 at the latest. This target goes beyond the target of 140 g CO_2/km provided for in the commitments of the car industry, leaving a "gap" of 20 g CO_2/km to cover. The car industry's commitment is to be achieved mainly through technical developments, and market changes linked to these developments. This leaves scope for further market changes being induced by the other instruments - in particular fiscal ones - which are part of the Community strategy[19]. The 20 g CO_2/km "gap", mentioned above, must be closed with the help of these other instruments, and the Council invited the Commission, on several occasions, to consider fiscal framework measures.

In the year 2000, the average level of CO_2 emissions from newly registered cars produced by members of ACEA, JAMA and KAMA was 172 g/km. According to a recent Commission report, based on monitoring figures on the implementation of these commitments, it appears that the car industry is making significant efforts to meet the target[20].

---

[14] Council conclusions of 25.6.1996.

[15] Communication from the Commission to the Council and the European Parliament: A Community Strategy to reduce CO_2 emissions from passenger cars and improve fuel economy, COM(95)689final.

[16] For details see http://europa.eu.int/comm/environment/co2/co2_home.htm

[17] Commitments made by European (ACEA), Japanese (JAMA) and Korean (KAMA) automobile manufacturers' associations to reduce average new passenger car CO_2 emissions, see COM(98)495final, COM(99)446 final, and Recommendations 1999/125/EC, 2000/304/EC, 2000/303/EC.

[18] Directive 1999/94/EC relating to the availability of consumer information on fuel economy and CO_2 emissions in respect of the marketing of new passenger cars (OJ L 12 of 18.1.2000, p. 16-23).

[19] COM(1998)495 final.

[20] COM(2001)643 final.

With the objective of contributing to the "third pillar" of the strategy, the Commission has established an "Expert Group on Fiscal framework measures" and it conducted a comprehensive study[21]. This chapter sets out the main conclusions of the study.

Based on model projections on road transport CO_2 emissions, it can be estimated that the CO_2 emissions would change in the period 1995 to 2010 as follows:

- without additional measures + 17%
- with car industries commitments being implemented (target 140 g/km)+7%
- with Community target being implemented (target 120 g/km) +3%

This means that if the 120 g/km target could be met the upward trend in total CO_2 emissions from road transport could be nearly broken and emissions could be more or less stabilised, around 1995 levels, somewhere between 2005 and 2010.

As far as the total CO_2 emissions from passenger cars are concerned, the picture is as follows:

- if car industry commitments are implemented (target 140 g/km), the CO_2 emissions of passenger cars could be stabilised;
- if the 120 g/km target were met, these emissions would go down by a few percentage points, as compared to 1995 levels. In absolute terms a total additional EU CO_2 emissions reduction of about 30 Mt could be achieved, compared to the 140 g/km target levels.

Therefore, to meet the 120 g/km target is of importance for the achievement of Community's Kyoto Protocol target.

[21] Study on fiscal measures to reduce CO_2 emissions from new passenger cars - A study undertaken by COWI Consulting Engineers and Planners AS, November 2001. This study is available under the following website address:http://europa.eu.int/comm/taxation_customs/taxation/car_taxes/co2_cars_study_25-02-2002.pdf

5.2. Fiscal measures, a tool for CO_2 emissions reduction

The study (COWI) confirmed that, irrespective of the considerable differences among national vehicle taxation systems:

- fiscal measures do have a potential in supporting the reduction of the average CO_2 emissions from new cars, in all the Member States that were analysed;
- the level of RT or ACT, in absolute terms, is not very relevant for the effectiveness of vehicle taxes with regard to CO_2 emissions of new cars[22]. Solely increasing the overall level of the existing tax rates, without changing the tax base, does not provide for a significant effect, within the boundary conditions (see explanatory note on Table 7 in the Annex;
- more significant reductions can be achieved, if the national taxation systems were designed in such a way that a CO_2 specific element was inserted in the existing tax basis of either or both RT and ACT;
- tax differentiation is the key parameter for improving the fuel efficiency of passenger cars;
- the highest CO_2 emissions reduction level, going up to 8,5%, has been calculated in DK, if both RT and ACT would turn into purely CO_2 based taxes and would be differentiated in a co-ordinated manner (see Table 7 in the Annex for a summary of the results);
- the highest possible CO_2 reductions can be achieved if efforts are focused on that vehicle tax, which, in absolute terms, has the higher level.
- modifications of RT or ACT do not lead to significantly different CO_2 reduction results. RT and ACT seem to be equally effective.

5.3. Tax differentiation based on CO_2 sensitive parameters

Tax differentiation has been identified as an important parameter for improving the overall fuel-efficiency of new cars. The design of tax differentiation should take into account the characteristics of national vehicle taxes and vehicle markets.

---

[22] The effect on total CO_2 emissions of vehicle fleet has not been studied. However, it is obvious that the type of vehicle tax, as well as the level of tax can have repercussions on the renewal of the fleet and consequently on CO_2 emissions.

- To give an example: if the ACT is based on the cylinder capacity of a passenger car, two particular vehicles of 1500 cc pay the same ACT, irrespective or their fuel consumption, weight, age or technology. Tax differentiation means that the owner of a fuel-efficient passenger car should pay lower ACT, compared to the owners of a similar but less fuel-efficient car. The total tax revenue for the state should, nevertheless, remain stable. Tax differentiation between these two cars should be sufficiently high, in order to provide a strong incentive to consumers in favour of the more efficient car.

- If RT and ACT are partially or totally CO_2 based, tax differentiation has more room for providing incentive to improve CO_2 efficiency.

- Currently only one Member State (UK) applies a CO_2 based ACT. A passenger car emitting less than 150g CO_2/km is charged by 159 EUR, while more polluting cars are charged by a tax amount increasing gradually to reach the level of 246 EUR for those cars emitting more than 185 g CO_2/km .

- In the Netherlands, from 1 January 2002, fuel efficient passenger cars have been awarded an energy bonus. This bonus is provided as a reduction of RT.

In the Commission's opinion vehicle taxation:

- is an important complementary instrument to support the realisation of the EU-target of 120 g CO_2/km for new cars by 2008-2010, and to contribute to the accomplishment of the EU engagements under the Kyoto Protocol.

- needs to establish a more direct relation between tax level and the CO_2 performance of each new passenger car. Vehicle tax differentiation has been identified as an important parameter for improving the overall fuel-efficiency of new passenger cars. Existing vehicle taxes should be replaced by taxes fully based on CO_2 emissions or, alternatively, a CO_2 sensitive element should be added to existing RT and ACT. Add-on elements would also allow taking into account other national environmental objectives, e.g. the early introduction of EURO IV standards.

The Commission is aware of the potential conflict between the revenue objective of vehicle taxation and other policy objectives. If RT and ACT were restructured in an environmentally friendly direction, revenues from these taxes could show a downward trend as a result of a successful environmental policy. However, this very much depends on the design of the restructured taxes, and on the way car buyers, and car drivers, react on new tax incentives. In order to ensure stable revenue, and to maintain the incentive function of these taxes, it may be necessary to amend the design, and the levels, of these taxes. Such amendments would also take into account the potential for revenue losses, due the expected higher fuel efficiency of future passenger car generations.

5.4. Company car taxation

Company cars are a significant proportion of new passenger cars sold each year, and of the total car fleet. So far, no single and generally acceptable definition has been established of what constitutes a "company car". This is due to the fact that the circumstances, and tax arrangements, differ significantly from one Member State to another. Generally speaking, company cars:

- tend to be 8 - 10% larger and more powerful than the national fleet average, and consequently more CO_2 polluting.
- normally have a higher mileage per year than the fleet average, and a higher contribution to total traffic levels, pollutant emissions and average fleet fuel consumption.
- remain in company's ownership for a period between one and three years, before being sold on to the private second-hand market.
- due to their type, and number, have an important impact upon the size and composition of the entire car fleet, and hence upon its CO_2 emissions profile.
- are less sensitive to retail price changes than private passenger cars.

Company cars are a significant proportion of all passenger cars (new and second hand). Of all cars sold in the main EU markets in 1999, sales of company cars formed between 35% and 45% (see Table 9 in Annex). Ireland and Italy are exceptions with 7,5% and 10% respectively. Company cars tend to be larger, and more powerful than the fleet average. This is partly explained by the fact that more affluent motorists (professionals, managers and company executives) for various reasons use many of them. In addition, tax treatment and other financial arrangements may reduce the real costs to buyers or drivers, encouraging a trend towards larger cars.

Although taxation on company cars varies considerably from one Member State to another, the arrangements generally provide for:

- *corporate tax* arrangements, which allow the purchase/leasing and running costs of the company cars to be deducted from the taxable profit and
- *income* tax has to be paid by the employee using the company car. Generally, the use of a company car is considered as a "benefit in kind", and the estimated car benefit is added to his personal income, and taxed in accordance with the national taxation system. To calculate the annual amount of this benefit, a rate, varying according to Member State, is applied on the purchase value of the company car (pre-tax price + RT + VAT). Its level ranges from 9% in Sweden and 12% in Germany up to a level of 25.5% in Ireland and 35% in the UK.

Moreover, the input VAT paid by a company when buying or leasing a company car, is in principle deductible, in so far as the car is used for the purposes of taxable activities (in certain Member States deduction is however subject to limitation). Taking into account the size and value of cars companies normally buy, deduction of

VAT may provide a strong incentive for them to buy such expensive, and as rule, less fuel-efficient, passenger cars.

Recent developments show that several Member States are revising their company car tax system. Three Member States impose charges on the supply of free fuels for private use (Ireland, Finland and the UK), while others apply a charge per km driven. A new company car taxation scheme is due to enter into force in the UK in 2002. According to this scheme, the income tax to be paid by the employee using the company car will partly be based on the CO_2 emissions of the car. This new scheme could provide useful experience, and serve as a best practice for future action in other Member States.

The Commission encourages companies to take into account the general transport and environmental policy objectives, when providing cars to their staff for commuting to work. It intends to amend Commission Recommendation on guidance for the implementation of Regulation No 761/2001[23] (EMAS) in order to ensure that the environmental impact of company cars is fully taken into the audit.

[23] OJ L 114, of 24.4.2001, page 1

6. CONCLUSIONS AND POLICY RECOMMENDATIONS

The EU passenger car market is fragmented into fifteen national markets, and this is partly due to very divergent policies in respect of car taxation. This raises a series of problems for both the European citizen and the car industry. The introduction of the Euro has started to bring greater price and tax transparency, and could increase pressure for more vehicle tax approximation. This Communication provides evidence that a number of policy measures and actions should be considered in the area of passenger car taxation, in order to provide definitive solutions for the problems faced by citizens and the car industry, and thus improve the functioning of the Internal Market and the benefits which EU consumers derive therefrom. Apart from this, the Communication has made clear that vehicle taxation can contribute to the achievement of the Kyoto Protocol commitments.

A. Removing tax obstacles in the internal market for passenger cars

1. Registration tax levels should be gradually reduced, with a view of RT stabilisation at low levels, and preferably with a view to its total abolition. This action should take place over a transitional period of about 5 to 10 years. It should take into account the specific conditions in each Member State.

2. A gradual *transfer of revenue* from RT to ACT, and to some extent to fuel taxes, should be decided. This transfer is feasible, and can take place in parallel with the reduction of RT, in a budget neutral context.

3. Action has to be taken in order to ensure a certain degree of ACT approximation among all Member States, in particular as regards tax bases. Reasonable ACT divergences would prevent car market fragmentation, and prevent increased tax avoidance in future.

4. The excise duty on diesel, used as fuel by passenger cars, should be gradually increased in view of its total alignment, in the medium term, to the excise duty applied on unleaded petrol. At the same time, ACT for diesel cars should be aligned to the ACT for petrol cars.

5. A *RT refund system* should be established without delay in all ten Member States currently applying a RT. This system should ensure, during the transitional period, a pro rata refund of the residual RT in all cases where a passenger car, registered in one Member State, is exported or is moved permanently to another Member State. Should such a system be adopted, it would resolve all problems relating to double payment of RT that the EU citizen faces today. The refund system should also apply in the case of cars moved permanently to another Member State in connection with a transfer of residence. The refund system would also have a positive influence on the export of used cars, because prices can be lower as a consequence of the refund of RT.

6. General rules with regard to the *method of calculation* of RT on used cars imported from other Member States should be established. This method of calculation of the residual amount of RT should also apply to the refund system.

7. General rules should be established with regard to the avoidance of double taxation of ACT.

B. Fiscal measures one of the tools for CO_2 emissions reduction of cars

1. Vehicle tax bases need to be restructured in order to establish a more direct relation between taxation levels and the CO_2 emissions of new passenger cars. Both RT and ACT should be turned into entirely CO_2 based taxes, or at least a CO_2 sensitive element should be added to both of them. This structural change is necessary in order to optimise the effect of taxation on the reduction of CO_2 emissions from new passenger cars. It should take into account the specific conditions in each Member State. For example if the RT in a Member State is already rather low, the transitional period during which the RT will be further reduced could be relatively short. In this case, it may not be worthwhile to carry through this structural change in the RT. The restructuring should then focus on the ACT, in a context of gradual approximation of tax bases.

2. All Member States should establish tax differentiation as an important parameter for making passenger car tax systems more CO_2 efficient and optionally to contribute to the reduction of other emissions. The optimal level of tax differentiation could differ from one Member State to another, taking into account the particular characteristics of each Member State's market.

3. Company car taxation has to take into account the general objectives of EU policies, and in particular, those of transport and environmental policies. Taxation should take into account the increasing importance of company cars, and provide a clear and strong incentive to companies to use more CO_2 efficient cars. In most Member States, existing corporate or income tax structures do not include such an incentive.

WAY FORWARD AND CONCLUSION

1. The Commission recommends that the Council approves the general principles mentioned under paragraphs A and B above and that the MS take into account these general principles when evaluating and revising their national vehicle taxation systems.

2 The Commission, based on these principles and in the light of the results of the consultation process, could submit proposals for Community legislation, which:

- in the short term establishes a *RT refund system* and general rules with regard to *the method of calculation of RT* on used cars, which are transferred between Member States;

- during a transitional period provides for the *gradual reduction of RT* to a low level, and preferably with a view to its total abolition; and,

- provides for the *restructuring and approximation of the ACT and RT tax bases*, in order to make these taxes more CO_2 efficient and more consistent with the internal market.