

Summary

Two key objectives identified by the new Commission are to reduce Europe's high level of unemployment and to continue Europe's leadership in reducing climate emissions. Ending the generous tax subsidies received by aviation is a way to do both.

Context

In the transport sector, a shift from labour to environmental taxes can reduce unemployment and emissions. Aviation receives an exemption from fuel duty and VAT, a loss to tax revenue which amounts to €40 billion every year¹. Ending this exemption and using the revenues to reduce Europe's high labour taxes would create employment by easing the cost of hiring and would curb the rapid increase in aviation emissions by creating a level playing field with other modes of transport.

“On pure tax policy grounds, the case for a generalised increase in taxes on international aviation is strong. Rates of tax are low at present, whereas there is quite persuasive evidence of significant cross-border damage from international air travel and, moreover, international air travel is in principle just as proper an object of indirect taxation as any other commodity.” (IMF, 2013)

High taxes and increasing emissions

Increasing aviation emissions

The EU has committed to an ambitious climate objective of a 40% reduction in emissions by 2030, as part of a reductions pathway needed to avoid a global temperature increase of above 2 degrees. While other sectors of the economy have made progress in reducing overall emissions, the aviation sector has more than doubled its emissions since 1990². As efficiency gains are becoming harder to achieve, and as sustainable fuels are not becoming available in sufficient quantity to make a meaningful impact, further measures are needed to avoid what is expected to be an almost doubling of emissions by 2030.

Labour taxes – highest in the world

Europe occupies the top 14 countries globally when it comes to taxes on labour as identified by the OECD, and 19 of its states are in the top 21³. In its Europe 2020 strategy, the Commission identified such levels as a burden on creating employment and in its European Semester recommendations (2014 and 2015) it called for a job-creating shift in taxation away from labour and towards environmental taxation⁴. One study has found that for every €1 billion euro in cuts to labour taxation, 10,000 jobs can be created⁵. Finding ways to cut labour taxes must therefore rank as a key objective for the EU and member states.

If we are to avoid aviation undermining Europe's climate objectives, we need to take concrete steps to arrest the growth in emissions from this sector.

¹ <http://www.transportenvironment.org/publications/does-aviation-pay-its-way>

² <http://www.transportenvironment.org/what-we-do/aviation>

³ <http://www.eea.europa.eu/publications/term-report-2014>

⁴ http://ec.europa.eu/economy_finance/economic_governance/the_european_semester/index_en.htm

⁵ Ekins, P., Resource Productivity, Environmental Tax Reform and Sustainable Growth in Europe, Anglo-German Foundation for the Study of Industrial Society, 2009 (p31)

Aviation's great tax break

Due to complex legal barriers, tax subsidies that were designed to encourage aviation when it was in its infancy continue to this day. These include a ban on fuel taxation for international flights enshrined in Air Service Agreements and, here in the EU, an outdated directive which makes it impossible to introduce VAT on cross-border aviation tickets.

These tax exemptions are causing a real and growing distortion between modes of transport. In one large member state, rail and bus prices have grown 15-20% since 2000 while aviation prices have decreased 40% over the same period⁶. As Europe moves to invest more and more in rail, this distortion will undermine the economic viability of these projects.

These exemptions are a subsidy which will continue Europe's reliance on fossil fuels. Already, 94% of transport relies on oil products, of which 90% is imported. Subsidies which exacerbate this dependence must be urgently ended.

By ending these exemptions, Europe can create a level-playing field for all modes of transport and can use the additional revenue to fund job-creating labour tax cuts. The best way to achieve this is at EU level, where one tax policy can be put in place for all 28 member states, reducing regulatory burden and confusion.

Taking action at EU level

Ending the fuel duty exemption

When civil aviation was in its infancy in the 1940s, the industry was granted a limited tax exemption under the Chicago Convention (the UN agreement to regulate the sector) for fuel on board arriving flights only. That exemption was deliberately expanded under Air Service Agreements (ASAs) at the behest of industry to include a prohibition on any taxation of fuel on international flights. As a result of poorly negotiated ASAs, the EU can now not even introduce fuel taxation on flights within its own borders. And incredibly, the EU-US Open Skies agreement includes a ban on fuel taxation on intra-EU flights, despite fuel taxation having existed in the US for several decades.

Ending the VAT exemption

Under outdated EU rules, passenger VAT is calculated according to where the trip takes place. So a Paris-Warsaw trip, if VAT was levied, would pay a portion to France, a portion to Germany, possibly some to the Czech Republic and the remainder to Poland. This is difficult but doable for rail, but impractical for aviation where flight paths change on a regular basis. For member states looking to introduce the sort of tax shift encouraged by the Commission, this is an unnecessary and archaic barrier.

An important step would be to change these restrictive VAT rules to one where VAT is levied according to the place of departure. In recent years we have seen VAT rules changed to take into account e-purchases, and the result is a simpler system that ensures more revenue for member states. Likewise, it is time to update these rules on passenger transport.

Conclusion

There is an urgent need to reduce Europe's emissions and its labour taxes, and the EU must identify concrete steps to achieve both. Changing fuel taxation and VAT rules is one way of achieving this, bringing in extra revenue to member states and creating a level playing field between modes of transport. The Commission must therefore propose legislative changes as a matter of urgency if we are to move towards a prosperous, low-carbon economy.

Further information

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⁶ <http://www.theyworkforyou.com/wrans/?id=2015-02-10.223954.h#g223954.r0>