Foreword

In the past years the EU budget fell short in delivering the necessary investments to face current economic, social and ecological challenges. On the contrary, the Mid-Term Review of the Multiannual Financial Framework (MFF) 2014-2020 shows: after a series of rigid budget-deals, the Union lacks sufficient financial means and flexibility for adequate responses to emerging crisis.

In contradiction with the spirit of the treaties, 86% of EU budget is today financed by member states’ national contributions. In consequence, EU budget negotiations have turned into a zero-sum game between national governments that focus on reducing their national contributions rather than on shared challenges and responsibilities leading to a fairer distribution of wealth for all Europeans. Furthermore, an opaque rebate system as well as insufficient national parliamentary oversight weaken the democratic accountability on how the EU budget is financed.

New ‘EU own resources’ could alter the structure of the EU’s revenues to achieve a more sustainable, sufficient and more democratic financing of the EU’s budget. At the same time we are convinced that in the face of the ecological challenges the EU is facing, policy makers need to create financial incentives to lower the use of natural resources and reduce \( \text{CO}_2 \) emissions. Such “Green Own Resources” unfold the transformative power of the EU budget and thereby help to achieve the energy and ecological transition that is underway.

The Working Group Budget of the Greens/EFA Group in the European Parliament has commissioned this study to take a closer look at the challenges and potentials of introducing Green Own Resources. The discussion on the introduction of new financing mechanisms for the EU budget is not new. Different factors, especially the lack of political will and majority on the side of the Council have hindered substantial reforms in the past decades. With this study we want to make a contribution on overcoming the stalemate in the reform debate, show-case concepts of Green own resources and provide Green stakeholders from different levels with arguments to address myths and contentions on Green Own Resources.

The time to introduce truly own green resources into the EU Budget is now! The current pressure on the EU budget, the upcoming BREXIT, as well as the beginning of the negotiations of the next MFF post-2020 in the next year open the window of opportunity for a fully-fledged reform. The next two years are crucial to make the income side of the EU budget more sustainable, more transparent, make the EU more autonomous and make better use of the EU Budget’s transformative power.

Helga Trüpel  
Ernest Maragall  
Monika Vana  
Indrek Tarand
Executive Summary

The EU budget: key instrument for a successful transition to a low-carbon society

The Paris Agreement establishes the global commitment to make “finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development” (article 2). At the same time the Sustainable Development Goals (SDGs) necessitate a paradigm shift in various social and economic areas. While Europe is preparing to put this vision into action, the EU budget with its EUR 143.5 billion volume, will need to become an important key enabler to get to net-zero emissions by mid-century. This applies to both the EU’s funding programmes and expenditures governed by the Multiannual Financial Framework (MFF), as well as to the way the budget is funded.

However, EU member states need to act as well, but their current fiscal systems are not ready to deliver a well-below 2°C GHG reduction target aimed for in the Paris Agreement: In 2012, labour taxes accounted for 51% of total tax revenue in contrast to a mere 6.4% revenue share from environmental taxes. Against EU member states’ pledges to green their tax systems, the ratio of environmental to labour tax revenue has deteriorated in the past years (see figure). Shifting taxation away from labour and towards more growth-friendly taxation, especially taxes on pollutants and polluters, has been an integral component of the Sustainable Development Strategy and the Europe 2020 strategy.

It follows that the EU own resource system, the revenue side of the European budget, is in need for reform. Most academics and politicians agree with the findings of the first assessment report of the High-level group on own resources (HLGOR) chaired by Mario Monti which has diagnosed that the financing system of the EU suffers from being too complex, non-democratic and crippled by nationalist net balance disputes. By the end of 2016, the group will present its proposal to reform the own resource system and put forward candidates to replace the direct national contributions which currently fund 86% of the budget. Among the candidates are also own resources based on environmental taxes and other fiscal instruments with a clear sustainability focus, candidates this report refers to as Green Own Resources. They could bring the financing system

Figure: Ratio of labour to environmental taxes, EU 28, 2002-2012

Note: Expressed in ratio of the share of labour taxes in total revenues from taxes and social contributions to the share of environmental taxes.

Source: Eurostat (2016a). Online data code: tsdgo410

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3 Whereas the sustainability of the EU budget can only be evaluated with a holistic view at both income and expenditure, this report looks only at options for reforming the EU’s revenue side, the own resources system. There are a number of inspiring studies critically assessing the climate mainstreaming of the EU MFF, notably FOE and CEE Bankwatch (2016), Milieu and EC (2015) and IEEP (2014).
of the EU in coherence with the EU’s long-term objectives on sustainable development.

An opportunity for reform

This study comes in a timely moment. In 2013, the European Parliament made its consent to the 2014-2020 MFF conditional on the reform of the EU’s own resource system. The interinstitutional High-level group on own resources (HGLOR) chaired by Mario Monti was given the mandate to deliver a proposal for a new way of financing the EU budget by the end of 2016. Their recommendations will feed into a Commission proposal to reform the revenue side of the EU budget which is expected to coincide with the negotiations for the upcoming MFF. Since the mid-term review of the current MFF has revealed that the EU is on a lower bound trajectory to deliver the 20% climate mainstreaming objective, more ambition is needed when preparing for the next EU budget period. In light of the recent ratification of the Paris Agreement by the European Parliament and the SDG Sustainability Agenda, the EU budget reform provides a unique opportunity to incorporate the EU’s long-term sustainability objectives as enshrined in its international commitments into its financial fabric.

Greening the EU budget: the potential of Green Own Resources

In order to accomplish the European transition towards a low carbon economy, the EU needs to set in motion a tremendous shift in investments over the upcoming decades. Full implementation of the climate pledges of the Paris Agreement requires the energy sector worldwide to invest EUR 12 trillion between 2015 and 2030 representing around 40% of total global energy sector investment. Additionally, the implementation of the Sustainable Development Goals necessitates annual EUR 4 to 6 trillion according to the UNCTAD. The current investment gap in Europe which partially stems from distortive market signals could prevent the EU from finding the most cost-efficient way to decarbonise by mid-century.

Green Own Resources address fiscal distortions that favour a fossil fuel-powered economy, incentivise more sustainable behaviour and provide the structural basis for a gradual, socially acceptable transition towards a low-carbon society. At the same time they can provide the EU with genuine own resources in the spirit of the Treaties and significantly reduce the share of national contributions to the budget.

Aim of the study: Debunking the myths

In spite of a wide pool of experience with environmental taxation, academic expertise calling for environmental tax shifts and the apparent policy inconsistencies which green taxes could effectively help to alleviate, European policymakers often face challenges communicating environmental taxes to crucial stakeholders. An effective communication strategy can support policymakers in overcoming this hesitation and in generating the necessary political support for a sustainable reform of the EU budget.

This study identifies four main communication barriers which proponents of Green Own Resources need to address. They relate to widespread contentions about environmental taxation among the electorate: (i) detrimental impact on competitiveness, (ii) regressive effect on social equity, (iii) trade-off between revenue stability vs environmental effectiveness and (iv)

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uncertainty about the respect of the subsidiarity principle.

This report discusses these contentions for eight Green Own Resource candidates, each contributing to a more socially, ecologically or economically sustainable European budget.

- EU Carbon Tax
- Border Carbon Adjustments
- Energy Tax
- Road Fuel Tax

- EU Air Ticket Tax
- EU Financial Transaction Tax
- EU Corporate Income Tax
- Fines of the Court of Justice

**Key messages in support of Green Own Resources**

The report seeks to develop counterarguments specific to each Green Own Resource to provide proponents with an inventory of key messages. These pro-arguments are then linked to specific target groups in the electorate, each with their own particular preferences, interests and concerns. The five specific target groups addressed in this study are the green community, citizens, local councillors, industry and member states.

The following table provides an overview indicating a set of key arguments per instrument and target group. The corresponding detailed key message can be found in the respective chapter on the Green Own Resource in question in part three of the study.
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<th>GREEN OWN RESOURCE CANDIDATES</th>
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<td>A Paris-consistent path for renewables</td>
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</tr>
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<td>Incentivise use of sustainable fuel</td>
</tr>
<tr>
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</tr>
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<td>Tax recycling for progressive distribution</td>
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<td>Improve air quality</td>
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<tr>
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<td>Social effects</td>
</tr>
<tr>
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<td>Sufficiency</td>
</tr>
<tr>
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<td>Progressive tax on flying</td>
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<td>United against tax avoidance</td>
</tr>
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<td>Credible market rules</td>
</tr>
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<td>Sustainable mobility</td>
<td>Legal certainty</td>
</tr>
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<td>EU budget consistency</td>
</tr>
</tbody>
</table>

- **ECONOMY**
- **SUSTAINABILITY**
- **SOCIAL**
- **EUROPE**
Contents

Foreword ............................................................................................................................... i
Executive Summary ........................................................................................................... iii
Abbreviations .................................................................................................................... 5

Introduction: Communicating the Greening of the EU Budget ........................................... 7

1 The current EU budget framework and its deficits ....................................................... 9
  1.1 The evolution of the EU budget – in a nutshell ....................................................... 9
  1.2 The legal framework of the EU budget ................................................................. 10
      1.2.1 Financial provisions of EU primary law ....................................................... 10
      1.2.2 Provisions on own resources in EU secondary law ...................................... 10
  1.3 The structure of the revenue side of the EU budget ............................................. 12
  1.4 The deficiencies of the current budgetary system ................................................. 13

2 Communicating Green Own Resources ..................................................................... 15
  2.1 How to address existing policy barriers ............................................................... 16
  2.2 Address needs and interest of target groups ....................................................... 23

3 Communicating Green Own Resource Candidates .................................................... 25
  3.1 EU Carbon Tax ....................................................................................................... 27
      3.1.1 EU Carbon Tax Profile ................................................................................. 27
      3.1.2 SWOT-Analysis for EU Carbon Tax .............................................................. 30
      3.1.3 Key messages for EU Carbon Tax ................................................................. 31
  3.2 Border Carbon Adjustments .................................................................................. 35
      3.2.1 Border Carbon Adjustments Profile ............................................................. 35
      3.2.2 SWOT-Analysis for Border Carbon Adjustments ........................................ 37
      3.2.3 Key messages for Border Carbon Adjustments .......................................... 38
  3.3 Energy Tax .............................................................................................................. 41
      3.3.1 Energy Tax Profile ....................................................................................... 41
      3.3.2 SWOT-Analysis for Energy Tax .................................................................. 43
      3.3.3 Key messages for Energy Tax ..................................................................... 44
  3.4 Road Fuel Tax ......................................................................................................... 49
      3.4.1 Road Fuel Tax Profile .................................................................................. 49
      3.4.2 SWOT-Analysis for Road Fuel Taxes ............................................................ 51
      3.4.3 Key messages for Road Fuel Taxes .............................................................. 52
3.5 EU Air Ticket Tax ................................................................................................................. 57
  3.5.1 EU Air Ticket Tax Profile ............................................................................................... 57
  3.5.2 SWOT-Analysis for EU Air Ticket Tax ......................................................................... 59
  3.5.3 Key messages for EU Air Ticket Tax ............................................................................ 60
3.6 EU Financial Transaction Tax ............................................................................................ 65
  3.6.1 EU Financial Transaction Tax Profile ........................................................................... 65
  3.6.2 SWOT-Analysis for Financial Transaction Tax ............................................................ 67
  3.6.3 Key messages for Financial Transaction Tax ............................................................... 68
3.7 EU Corporate Income Tax ................................................................................................. 71
  3.7.1 EU Corporate Income Tax Profile ................................................................................. 71
  3.7.2 SWOT-Analysis for EU Corporate Income Tax ............................................................ 73
  3.7.3 Key messages for EU Corporate Income Tax ............................................................... 74
3.8 EU Court of Justice Fines .................................................................................................. 77
  3.8.1 CJEU Fines Profile ....................................................................................................... 77
  3.8.2 SWOT-Analysis for CJEU Fines .................................................................................. 79
  3.8.3 Key messages for CJEU Fines ..................................................................................... 80
Conclusion: spreading the word of Green Own Resources ......................................................... 84
References .................................................................................................................................. 85
Glossary ..................................................................................................................................... 92
Annexes ..................................................................................................................................... 95
  Annex I: Development of EU budget revenue 1970-2016 ........................................................ 95
  Annex II: Sequential calculation of the EU budget ................................................................. 97
  Annex III: Policy options for compensatory measures ........................................................ 98
  Annex IV: EU Air Ticket Tax – list of countries with existing and abolished air ticket tax ... 99
  Annex V: Exceptions to the non-assignment rule ................................................................. 100
List of figures

Figure 1: Revenue and expenditure of the EU budget 2016................................................................. 7
Figure 2: Composition of EU revenue 1970-2016 .............................................................................. 9
Figure 3: Overview of the legal framework governing the budgetary system of the European Union .......... 11
Figure 4: Observed globally averaged combined land and ocean surface temperature anomaly 1850–2012 ............. 15
Figure 5: Ratio of labour to environmental taxes, EU 28, 2002–2012 ...................................................... 19
Figure 6: Exposures of European financial institutions to fossil-fuel firms (in billion EUR) .................................. 45
Figure 7: Gross inland consumption, EU-28, 1990–2014 in percentage share of total consumption .................. 47
Figure 8: EU and other major players in world-wide trade in motor cars in 2010 ............................................. 53
Figure 9: Gasoline/diesel tax rate ratios in EU member states compared to CO2-neutral ratio in 2015 ................. 54
Figure 10: Revenue from corporate income tax as a percentage of GDP in Eurozone countries....................... 75
Figure 11: Sequential calculation of the EU budget .................................................................................. 97
Figure 12: Policy options to avoid negative distributional effects of ETR on private households ..................... 98

List of tables

Table 1: Overview of revenue potential of Green Own Resource candidates .............................................. 25
Table 2: Key messages per target group supporting an EU carbon tax as a Green Own Resource .................. 31
Table 3: Key messages per target group supporting BCAs as a Green Own Resource ................................. 38
Table 4: Key messages per target group supporting energy tax as a Green Own Resource ........................... 44
Table 5: Key messages per target group supporting road fuel tax as a Green Own Resource ......................... 52
Table 6: Key messages per target group supporting an EU air ticket tax as a Green Own Resource ................ 60
Table 7: Key messages per target group supporting an EU FTT as a Green Own Resource .......................... 68
Table 8: Key messages per target group supporting EU CIT as a Green Own Resource ............................ 74
Table 9: Key messages per target group supporting CJEU fines as a Green Own Resource ........................... 80
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Abbreviations

ATP     Aggressive tax planning
BEPS    Base erosion and profit shifting
CCCTB   Common consolidated corporate tax base
CIT     Corporate income tax
CO₂     Carbon dioxide
CORSIA  Carbon Offsetting and Reduction Scheme for International Aviation
CJEU    Court of Justice of the European Union
dg      Directorate General
EBA     European Banking Authority
ecc     European Commission
ECSC    European Coal and Steel Community
EEA     1) European Economic Area, 2) European Environmental Agency
ECC     European Economic Community
EESC    European Economic and Social Committee
EEX     European Energy Exchange
efr     Environmental Fiscal Reform
efsf    European Financial Stability Facility
eiopa   European Insurance and Occupational Pensions Authority
ep      European Parliament
esa     European System of National and Regional Account
esd     Effort Sharing Decision (406/2009/EC)
esma    European Securities and Markets Authority
esr     Effort Sharing Regulation
etd     Energy Tax Directive (2003/96/EC)
eu      European Union
eua     EU emission allowances
eucit   European Union corporate income tax
eu ets  European Union Emission Trading Scheme
eur     Euro (European Monetary Unit)
fat     Financial activities tax
ftt     Financial transaction tax
GBP     British Pound Sterling
GDP     Gross domestic product
gj      Gigajoules
GMBM    Global Market-Based Mechanism
gni     Gross national income
gnp     Gross national product
ghg     Greenhouse gas
ghge    Greenhouse gas emissions
gni     Gross national income
gnp     Gross national product
hlag-st High Level Advisory Group on Sustainable Transport
hlgor   High-level group on own resources
icao    International Civil Aviation Organization
ifta    International Fuel Tax Agreement
imf     International Monetary Fund
mbi     Market-based instrument
mep     Member of the European Parliament
mff     Multiannual financial framework
| **MNE**  | Multinational enterprise |
| **MS**   | EU member state          |
| **NOx**  | Nitrogen oxides          |
| **OECD** | Organisation for Economic Cooperation and Development |
| **ORD**  | Own-Resources Decision (2014/335/EU) |
| **RAL**  | ‘Reste à liquider’ - outstanding commitments |
| **SDGs** | Sustainable Development Goals |
| **SME**  | Small and medium-sized enterprise |
| **tCO₂** | Tonne carbon dioxide     |
| **TEU**  | Treaty on European Union |
| **TFEU** | Treaty on the functioning of the European Union |
| **TOR**  | Traditional own resources |
Introduction: Communicating the Greening of the EU Budget

The Paris Agreement and the UN Sustainable Development Goals (SDGs) call for a paradigm shift in the way in which the EU is set up for 2030, 2050 and beyond. Article 2 of the Paris Agreement underlines the need to make “finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development”\(^9\). While Europe is preparing to put this vision into action, the EU budget will need to become an important enabler to get to net-zero emissions by mid-century.

A key investment tool comprising a volume of EUR 143.5 billion, the EU budget is crucial for providing European public goods such as climate and environmental protection, creating more social equity and economic cohesion or developing a cross-border research community.

Yet, the EU budget currently suffers from a number of constraints. One relates to its financial limitations. While the competences of the European Union grew significantly, especially in light of the financial and banking crisis, the EU budget shrank. Today, in 2016, it accounts for around one per cent of EU GDP or half of Germany's federal budget\(^10\).

Simultaneously, the EU budget has become too complex over the years and has diverted from its original intended design. This development has not only hampered democratic accountability, but also reduced the budget autonomy of the Union. While the share of truly genuine ‘own resources’, i.e. funding streams under the EU’s direct control, decreased from over 65% in 1976 to merely 12.9% in 2016, 86% of the EU’s total revenue are currently de facto national contributions\(^11\). This shift goes against the founding treaties of the Union which envisioned a directly controlled funding model based on own resources.

Figure 1: Revenue and expenditure of the EU budget 2016

Note: Broken down according to category, in percentage share of total budget (EUR 143 billion).


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\(^11\) Taken together, the share of the statistical VAT- and GNI-based revenues is more than 6 times larger than the proceeds from Traditional Own Resources, the EU’s truly genuine revenue. European Commission (2016a). Definitive Adoption (EU, Euratom) 2016/150 of the European Union’s general budget for the financial year 2016; and European Commission (2009). Financial Report EU budget 2008. Publication and accompanying dataset.
This predominance of national contributions in the budget has increasingly led to intergovernmental debates about each country’s net balance and about who gets their fair share. The debate has reinforced the perception among citizens that the EU is a costly burden rather than a tool for positive change and the common good.

It is time for the EU to renovate its outdated budget structure and to bring it in coherence with its long-term policy objectives. New Green Own Resources based on sustainability-enhancing instruments that can effectively tackle the structural budgetary challenges while providing for a clear pathway towards sustainable development could make this necessary transformation possible.

The European Parliament will play a vital role in this process\(^\text{12}\). Not least, it was the European Parliament which made its approval of the last long term EU budget (the Multiannual Financial Framework – MFF) conditional on the launch of a reform process of the own resource system that led to the establishment of a High-level group on own resources (HLGOR) chaired by Mario Monti in 2014\(^\text{13}\).

Building on a short overview of the current system of financing the EU budget, including a section on its main deficiencies (chapter 1), the report introduces the concept of Green Own Resources and its main rationale and identifies the main communication barriers as well as strategies to address them effectively (chapter 2). The third part covers the eight Green Own Resource candidates, briefly presents their potential to add to the EU’s sustainability agenda and provides the main key messages tailored to specific target groups for each instrument (chapter 3).

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1 The current EU budget framework and its deficits

1.1 The evolution of the EU budget – in a nutshell

Over the years the system of financing the European Union has evolved into a complex structure characterised by the subsequent inclusion and increase of non-genuine own resources and the expansion of convoluted systems for national rebates and exceptions. The following section will briefly outline some milestones in the evolution of the current system as well as its main characteristics.

After the European Coal and Steel Community (ECSC), founded in 1951 as a predecessor to the EU, had a genuine system in place for generating its own revenue, the Treaties of Rome establishing the European Communities in 1957 did not foresee the establishment of a system of own resources until the creation of a common tariff system.

In 1970 a system of own resources was introduced first comprising two resources: the so-called traditional own resources (TOR), revenues generated by customs duties and agricultural levies and a second revenue element derived from a statistical value-added tax (VAT) base. However, both resources proved to be insufficient in replenishing the entire EU budget. Thus, a third source of own resource based on the gross national product (GNP), later the gross national income (GNI) of each member state was introduced in 1988. As the share of the first two resources continued to shrink, the GNI-based resource became the main revenue source for the EU budget outpacing the share of TOR already by 1993 and the one of VAT-based resources in 1998.

Figure 2: Composition of EU revenue 1970-2016

Source: GBE illustration. For more details on data please see annex I.
1.2 The legal framework of the EU budget

The EU’s budgetary system is embedded in a distinct legal framework governed by (i) the financial provisions of EU primary law as enshrined in the Treaties, (ii) secondary legislation and interinstitutional agreements.

1.2.1 Financial provisions of EU primary law

Articles 310 to 325 of the Treaty on the Functioning of the European Union (TFEU) contain the main rules concerning the EU’s general budget, budgetary principles, its own resource system, the multiannual financial framework, the annual budget, implementation and discharge and combatting fraud. Article 310 establishes the six general principles of the Union’s financing system which are unity, universality, equilibrium, annuality, specification and sound financial management. Article 311 TFEU sets out the procedures to adopt the Own-Resource Decision (ORD).

1.2.2 Provisions on own resources in EU secondary law

EU secondary legislation governing own resources mainly comprises the Own-Resources Decision (ORD), the Implementing Regulation and the ‘making-available Regulation’.

The Own-Resources Decision (ORD)

The ORD can define new own resources and abolish old ones. The adoption of the ORD is subject to a special legislative procedure under secondary law. First, it requires unanimity in the Council while the European Parliament plays only a consultative role. Second, article 311 states that the decision needs to await approval by member states “according to their constitutional requirements”. In many cases this entails the involvement of national parliaments which gives the ORD almost the legal status of EU primary legislation. The most recent ORD was adopted on 26 May 2014. As it is still subject to ratification it will apply retroactively from 1 January 2014.

The Implementing Regulation

The Implementing Regulation specifies the implementing measures such as calculation and budgeting of the balance or control and supervision measures as contained in article 9 of the ORD.

The ‘making-available’ Regulation

The ‘making-available’ Regulation sets out the methods and procedure for making available the traditional, VAT and GNI-based own resources and on the measures to meet cash requirements.
Figure 3: Overview of the legal framework governing the budgetary system of the European Union

THE BUDGETARY SYSTEM OF THE EUROPEAN UNION

ANNUAL BUDGET
- TFEU Art. 314-315
  Budgetary Procedure
- TFEU Art. 317-319
  Implementation and Discharge
- Financial Regulation
  Regulation No 966/2012
- Rules of Application
  Commission Regulation No 1286/2012

OWN RESOURCES
- TFEU Art. 311
  On the Own-Resources Decision (ORD)
- Own-Resources Decision (ORD)
  Council Decision No 2014/335
  - Defines and establishes categories of GIs and methods of their calculation
  - Sets down ceilings for payments and commitment
  - Principles of current correction mechanisms
- Implementing Regulation
  Council Regulation No 608/2014
- 'Making-available' Regulation
  Council Regulation No 609/2014

MULTIANNUAL FINANCIAL FRAMEWORK
- TFEU Art. 312
  Multiannual Financial Framework
- MFF Regulation
  Council Regulation No 1311/2013

CURRENT REVENUE COMPONENTS
(percentage for 2016 budget)

OWN RESOURCES
- Other revenue + surplus (1.1%)
- Traditional own resources (12.9%)
- VAT-based own resources (13.1%)
- GNI-based own resources (72.9%)

LEGAL FRAMEWORK
- EU Primary Law
- EU Secondary Law
- Ordinary Legislative Procedure
- Adoption requires EP consent
- EP is consulted
- Delegated Regulation
1.3 The structure of the revenue side of the EU budget

EU budget revenue can be divided into two categories: own resources and other revenue. While EU own resources, which account for 98.9% of the EU’s total revenue, are determined by the ORD, other revenue constitutes the sum of various miscellaneous revenue. Own resources are currently financed through three revenue sources. The following section gives an overview of the main characteristics of each own resource.

A) Traditional own resources (TOR)

Traditional own resources (TOR) are based on proceeds from customs duties, agricultural duties, and sugar and isoglucose levies imposed on economic operators. Traditional own resources can be regarded as the most genuine direct revenue stream of the European Union, since the Union enjoys exclusive competences in the area of customs union. The duties themselves are derived from the establishment of the European Single Market with a common custom code and external tariff for non-member countries. In spite of being intended to be the main funding source of the Communities, the share of these genuine own resources has continuously decreased in recent decades, accounting for only 12.9% of the EU’s total revenue in 2016.

In addition, member states retain a share of the TOR as collection costs, amounting to 20% of the revenue.

B) VAT-based own resources

In order to compensate for the diminishing revenue generated by the traditional own resources, the ORD of 1970 introduced a second own resource based on member states’ VAT base. First accrued in 1979, it is calculated according to a specific harmonised rule. Today, the VAT-based resource accounts for 13.1% of the EU’s total revenue.

The 2014 ORD established a uniform call rate of 0.3%, but reduced rates for certain member states remain as a derogation to the general rate. Furthermore, VAT bases are capped at 50% of GNI in order to avoid any regressive effects of this resource which may be higher and thus penalising poorer countries with a higher share of domestic consumption.

C) GNP/GNI-based own resource

In view of the insufficiency of TOR and VAT-based own resources, the 1988 ORD introduced a third own resource element. In the past decades this GNI-based own resources has become the most important own resources with the largest share among all three resources, although it is far less genuine in nature and rather constitutes national contributions in disguise.

The GNI-based resource is also known as the ‘residual’ resource as its size is calculated after both the TOR and the VAT-based resources are determined and added to the proceeds from other revenue and the surplus from previous years are accounted for. Therefore, the share and size of the GNI-based resource is determined by the

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19 These various revenues consists inter alia of revenue accruing from persons working with the institutions and other EU bodies, Interest on late payments and fines, revenue from EU borrowing and lending operations etc.

20 ORD 2007 and 2014 defines them as revenue deriving from ‘levies, premiums, additional or compensatory amounts, additional amounts or factors, Common Customs Tariff duties and other duties established or to be established by the institutions of the Communities in respect of trade with non-member countries... as well as contributions and other duties provided for within the framework of the common organisation of the markets in sugar’.

21 Initially these costs amounted to 10% of total traditional own resources. The deducted share was later increased to 25% in 2001, but will be reduced to 20% after the ORD 2014 enters into force.

22 The reduced VAT call rate for the period 2014-2020 is 0.15% and applies to Germany, the Netherlands and Sweden.
difference between the appropriation ceilings, the overall budget ceilings determined in the MFF, and the sum of all other revenue. Through this procedure, an equilibrium ex ante of the EU budget can be guaranteed which ensures that the European budget cannot run a deficit\textsuperscript{23}.

**National exceptions and rebates**

Several financing exceptions add to the complexity of the aforementioned system.

The UK rebate, the largest exception in the budget was introduced at the Fontainebleau summit in 1985 to compensate for the UK’s perceived disadvantages in receiving Community funding\textsuperscript{24}.

The rebate guarantees that the UK is reimbursed 66\% of this budgetary imbalance. The cost of this correction is shouldered by the other 27 member states.

In addition, the ORD of 2014 also grants special exceptions to other individual member states in the form of lump sums for the period 2014-2020: EUR 659 million for the Netherlands, EUR 185 million for Sweden and EUR 130 million for Denmark. Lump sums granted to Austria will phase out over three years, amounting to EUR 30 million in 2014, EUR 20 million in 2015 and EUR 10 million in 2016.

1.4 The deficiencies of the current budgetary system

The budget structure and its unintended evolution has sparked a long debate about the need to reform the EU own resource system. In 2013, the European Parliament approved the 2014-2020 Multiannual Financial Framework (MFF) only under the condition of an interinstitutional agreement to reform the own resource system. This agreement led to the establishment of a High-level group on own resources (HLGOR) in 2014 with the mandate to develop options for a future financing system of the EU by the end of 2016\textsuperscript{25}.

The HLGOR consists of ten members, three members per institution under the chairmanship of Mario Monti. In December 2014, the group presented its first assessment report, stipulating the main deficiencies of the current budget which a new reformed financing system will need to overcome. The following overview of the current EU budget’s deficits is partially based on the HLGOR’s evaluation included in its first assessment report.

**A) Complexity and lack of transparency**

Due to the large number of exceptions and rebates granted to individual countries, the current own resources system is overly opaque and does not provide a comprehensive, coherent and transparent account of how the EU is financed.

This damages democratic oversight and feeds into the perception of the EU as a distant bureaucratic structure with few links to the everyday life of its citizenry. A simplified future budgetary structure should focus on the link between the EU and its citizens.

**B) The demise of genuine own resources**

A key term in these negotiations is the notion of the ‘juste retour’ referring to the focus of national governments to reclaim their fair share in returns from European integration. This tit-for-tat logic treats the European project as a zero-sum game neglecting the investment and spill-over potential

\textsuperscript{23} For an illustration of the sequential budgeting and the GNI-based own resource in its role as the residual resource, see annex II.

\textsuperscript{24} The rebate is calculated as the difference between the percentage share of the UK in EU expenditure paid to the member states (total allocated expenditure) and the UK share in total VAT and GNI resources payments. This difference in percentage points is then multiplied by total allocated expenditure.

of European funding and providing worrisome ammunition for populist politicians across Europe. A reinvigoration of genuine own resources could counteract this trend.

C) Insufficient parliamentary oversight

As mentioned before, the current composition of the EU budget with more than 80% stemming directly from non-genuine resources is in contradiction with the Treaty of the Functioning of the EU (TFEU) which foresees for the Union to be financed “wholly from own resources”. The excess of de facto national contributions gives disproportionate leverage to member states and thus the Council vis-à-vis the European Parliament during EU budget negotiations.

This lack of parliamentary ownership also extends to the national level. As stressed in the HLGOR first assessment report, national parliaments rarely debate EU own resources in the plenary.

D) Late payments

In the past years the number of late payments and unpaid bills, the so-called ‘payment backlog’, has dramatically increased to EUR 24.7 billion at the end of 2014. The case of late payments underlines that a budget mainly funded through member state contributions runs the risk of being held captive against the backdrop of national budget consolidation. New resources need to ensure a higher degree of budgetary autonomy of the European Union in order to guarantee that EU programmes can deliver.

E) The absence of steering effects of EU revenues

The large majority of the components of the current budget system is statistical and does not mirror any European policy with specific added value. If resources capable of addressing certain market failures would be deployed, the own resource system could thus achieve a double dividend in guaranteeing sufficient resources and in bringing the EU budget in line with policies closer to citizens by delivering European public goods and a higher EU added value. This could, according to the European Commission, support – and be closely linked to – “the achievement of important EU or international policy objectives, for instance in relation to development, climate change or the financial markets”.

Persisting market failures hamper urgently needed investments. Europe is experiencing a negative long-term trend in investments which risks to exacerbate due to the focus on austerity measures throughout the economic crisis. Green Own Resources can pave the way for higher and more sustainable investments. In this vision the European budget could create synergies between the Union’s current international sustainability commitments as well as its internal mid- and long-term energy and climate objectives.

26 According to the European Commission, this is mainly due to two developments. After the financial crisis, the Council unanimously decided to soften budgetary rules which previously provided strict requirements on the timing of payment claims for Cohesion policy programmes. In the area of Cohesion policy, this softening led to a cyclical increase of payment claims at the year-end which amounted to an unprecedented amount of EUR 61 billion in the end of 2013. At the same time, payment ceilings were lowered in the MFF 2014-2020 which entailed a particularly drastic reduction of payment appropriations of EUR 8 billion in 2014. European Commission (2015a).


28 In particular with regards to Article 2 of the Paris Agreement on ensuring that financial flows are better exploited to reach the 2°C/1.5°C target and in light of the attainment of the Sustainable Development Goals (SDGs).
2 Communicating Green Own Resources

The European Union needs to prove that it is capable of providing solutions to the multiple profound crises it is currently facing by safeguarding its social market economy, realising the transition towards a decarbonised society and guaranteeing economic and social stability. Green Own Resources could make the EU budget consistent with this trajectory as they can activate the systemic steering effects of the EU budget that are necessary to transform the European economy into a sustainable low-carbon society. And time is pressing.

Europe needs to act now if it wants to implement its ambitious decarbonisation targets needed to prevent the consequences of climate change from becoming “severe, pervasive and irreversible” as emphasised by the IPCC 2014 Synthesis Report.

Robust scientific evidence based on modelling exercises, policy analysis, evaluations of actual tax measures on the ground and successful implementation of EFRs in the past 30 years at national level could serve as a fruitful example for a reform of the EU budget.

Yet, when it comes to concrete policy steps, European politicians are still hesitant to act and not only risk missing the EU’s medium- and long-term climate targets, but also jeopardise Europe’s position as a global leader in low-carbon technology. An effective communication strategy can help to overcome this hesitation and generate

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the necessary political support for a sustainable reform of the EU budget. Reform proponents need to develop clear and comprehensive messages to convince different parts of the electorate, stakeholders and political partners, addressing their particular concerns and interests. These key messages should therefore be built on the following:

1. Analyse existing policy barriers and obstacles
   There is a widespread persistence of essential concerns about key features of Green Own Resources. The systemic changes needed for a success of Europe’s climate policy require strong and enduring electoral support. However, policymakers often have tremendous difficulties in gaining this support for concepts that involve public budgets, taxation or even the European Union as such. Proponents of Green Own Resources need to be aware of these contentions and provide appropriate counter-arguments.

2. Identify appropriate frames and narratives
   Increasing the share of Green Own Resources in the European budget has a wide range of direct and indirect consequences, not only of budgetary, but also of a social, ecological and macroeconomic, nature. Building on the experience with previous initiatives to promote green taxation and the obstacles identified, policymakers need to develop a set of different narratives which address the existing concerns about Green Own Resources and offer plausible evidence-based alternatives.

3. Address needs and interests of specific target groups
   Experiences with national tax reforms underline the importance of broad based, cross-party support as well as approval of key stakeholders. Thanks to forerunner countries, there is now a rich evidence base on the benefits and design options of environmental fiscal instruments. This understanding however largely remains in academic and policy expert circles and is not sufficiently debated in the broader public. Thus, key messages need to be tailored to distinct target groups and should address their specific concerns and needs.

The following section will look at these aspects in more detail. The first part discusses main policy obstacles and widespread concerns about green tax instruments, and provides alternative narratives and general counterarguments. The second part focuses on specific target groups crucial to forge a broad support base for Green Own Resources.

2.1 How to address existing policy barriers

The reform of the EU own resource system and the discussion of tax-based EU budget components require a broad public debate on the future direction of European integration. On the national level, experience with implementing Environmental Fiscal Reform (EFR) can inform the European debate on Green Own Resources and help understand the potential dynamics, obstacles and opportunities that concrete proposals might encounter. Since EFR initiatives also deal with concepts which are not very popular among the electorate such as taxation and the idea that long-term objectives are pursued through short-term costs, they can provide insightful examples to the Green Own Resource debate.

Experience with EFR in Europe stretches over a period of more than thirty years. Although each country has its unique political and cultural context
in which reform proponents have to forge the necessary political consensus, several main contentions which are also likely to be brought up against Green Own Resources can be identified across EU member states. They refer to green taxes’ effects on competitiveness, environmental effectiveness, revenue stability and social equity. In the case of Green Own Resources, an additional often-cited concern refers to the subsidiarity principle. The following section briefly describes each widespread concern and provides general counterarguments based on evidence and experience gained from decades of EFR.

A) Economic dimension

Widespread concern:
“Environmental taxes are bad for economic growth. They are detrimental to the international competitiveness of domestic industries and products.”

A reoccurring argument against environmental taxes is their alleged harmful effect on competitiveness. Underlying this concern is the assumption that if one country unilaterally raises environmental tax rates (especially energy and carbon taxes), the resulting increase in cost of production will put domestic products at a price disadvantage in relation to goods on the global market.

Little evidence on negative impact on competitiveness

There is no evidence that environmental taxation is per se bad for economic growth and international competitiveness. If Green Own Resources are part of a genuine tax shift there is no direct link to underpin this assumption. Revenue-neutral fiscal reforms which entail compensatory measures such as a reduction in labour taxes can even be growth-enhancing as they stimulate output and production due to general lower costs of labour.

In practice one has to differentiate between different levels of competitiveness. Individual firms and industry sectors need to ensure that their products and market shares remain able to compete in local and international markets. For countries, competitiveness entails that they can continue engaging in international trade with a moderate balance of payments and favourable levels of national income and employment. On a regional scale, Europe needs to ensure that it remains competitive as a global player in the world economy inter alia by anticipating technological trends and by providing consistent and credible signals to international investors about its future development.

Sectoral concerns about competitiveness usually entail that stricter environmental law could drive out local industries due to higher production costs, a process referred to as carbon leakage. However, a 2013 study investigating the impact of the EU ETS on forcing domestic firms to relocate their production has found “no evidence of carbon leakage as defined by the ETS Directive”30. This could be due to the fact that the ETS as well as many environmental tax initiatives have granted special treatment to energy-intensive industry sectors and that measures have been generally very modest or were gradually introduced to provide sufficient predictability and flexibility for adaptation.

The overall effect on national competitiveness is influenced by a number of design factors, for example the existence of tax exemptions or differentiated tax rates for industry and households or the provision of social equity measures compensating for revenue losses of lower-wage segments of the work force as well as social security measures. Actual evidence of negative impacts of EFR on national

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competitiveness is very scarce as such a reform was usually implemented with special tax provisions protecting industry sectors that were deemed most vulnerable. On the contrary, experience from the Danish CO₂ tax shows that it has indeed helped Denmark to secure its place as one of the most competitive and energy efficient economies in the world31. Scandinavian countries are a good example of high tax rates going hand in hand with a low-carbon social welfare state and a competitive economy.

The parameters that determine Europe’s global competitiveness are not static. If the cost of carbon will increase – which in the medium-term is inevitable – GHG emissions will become an ever-growing liability for economies across the world. Europe is at the crossroads and needs to make sure that its markets and producers are prepared to take the global lead in a low-carbon world market. This requires large-scale infrastructure investments as well as divestment measures but also compensation measures and re-skilling programmes for employment losses. Green Own Resources can give important signals to steer these investments and facilitate the transformation of the European economy into a more sustainable economic model.

Towards low-carbon competitiveness

Decarbonising the European economy will be impossible without a large-scale shift of private and public investment towards low-carbon infrastructures. The current price signals, not accounting for environmental externalities, are still set to incentivise unsustainable market behaviour. Green Own Resources could be a game changer, encouraging member states and the EU to develop more cost-effective transformative investment frameworks needed to make the EU “fit for Paris”, or in other words, to implement article 2 of the Paris Agreement and making “finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development”.

The reform of the EU budget is an enormous opportunity to align both EU revenue and expenditure with the EU’s main long-term priorities. EU funds, especially in the less developed regions in central and Eastern Europe need to boost clean development efforts. Investments in energy savings, resource efficiency and clean energy production need to increase significantly in order to overcome fossil fuel dependency.

Evidence shows that climate change policies can increase competitiveness in the long term by encouraging greater innovation and efficiency. In the last decade, jobs in the green sector have increased across the EU, with employment growing by 20% even during the recession years32.

Achieving the tax shift

The European Union and its member states have pledged to achieve ambitious targets to bring the EU on a pathway towards sustainable development. However, the EU’s current fiscal systems are not fit for purpose to deliver the net-zero target aimed for in the Paris Agreement: in 2012, labour taxes accounted for 51% of total tax revenue in contrast to a mere 6.4% revenue share from environmental taxes33. Shifting taxation away from labour and towards more growth-friendly taxation, especially taxes on pollutants and polluters, has been an integral component of the Sustainable Development Strategy and the Europe 2020 strategy.

33 Figure for EU 2012. Eurostat (2016a). Shares of environmental and labour taxes in total tax revenues from taxes and social contributions. Online data code: tsdgo410.
However, tax shifts have stagnated over the past 10 years and on average, the ratio between environmental and labour tax has even worsened. In 2000 revenues from labour taxes were on average about 6.2 times higher than revenues from environmental taxes, while in 2011 they were 8 times higher clearly running against the EU’s commitment to enhance the ‘greening of the taxation systems’.

Boosting member states’ budget consolidation

Green Own Resources can contribute to simultaneously achieving the double dividend of an Environmental Fiscal Reform in order to consolidate national budgets in a cost-efficient way, and environmental objectives. Under the budgetary constraints created by austerity policy, high unemployment rates, especially in Southern Europe and excessive levels of energy dependence of 53.2% of the EU-28 persist. Regrettably, environmentally harmful activities are still heavily subsidised through public budgets. Across the EU fossil fuels are subsidised by up to EUR 329 billion annually. This represents more than double the EU Annual Budget and includes up to EUR 42.8 billion that member states and citizens have to pay to compensate for the negative social and health impacts. Correcting these huge market failures would not only improve economic efficiency, but also raise additional revenues which could help inter alia mitigating budget deficits. Inaction however has a high societal cost as polluters do not pay for the damage they cause.

B) Sustainability dimension

Widespread concern:

“Environmental taxes cannot generate stable revenue because they make consumers change their behaviour over time.”

A third concern is that tax measures which intend a change in the behaviour of all market actors ultimately undermine their own tax base. A key objective for any Pigouvian tax is that it is based on units considered socially harmful (e.g. tonnes of CO₂ equivalents in the case of the carbon tax) in order to internalise their uncovered costs and disincentive their use throughout the economy. This entails that there is an alleged inherent trade-off between stable tax return and environmental effectiveness.

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35 Long-term unemployment remains high in crisis-torn countries such as Spain and Greece exceeding 10% for four subsequent years and EU 28 energy dependence. Eurostat (2016b). Energy dependence. Online data code: Code: tsdcc310.
38 For more details see the “Carbon and Energy Tax Reform in Europe” (CETRIE) report which reveals that carbon and energy taxation may raise significant revenues while having a less detrimental macro-economic impact than other forms of indirect and direct taxation. Vivid Economics (2012). Carbon taxation and fiscal consolidation: the potential of carbon pricing to reduce Europe’s fiscal deficits. Report by Green Budget Europe. Accessed 01.10.2016.
Addressing revenue stability

Again, such considerations cannot be generalised for all types of environmental taxes, but they depend primarily on elasticity. Energy products have a very low price elasticity of demand – ranging between 0 and -1 – meaning that consumer demand is unlikely to diminish substantially even if a new tax increased the total price of the product. In such cases the targeted environmental damage can be reduced while tax returns do not diminish over time. This is also the case for road fuel taxation as the consumption levels of motor fuel are fairly stable.

For other taxes such as the carbon tax, for which there seems to be an inherent trade-off between revenue and effectiveness, flexible, progressively increasing rates alongside a clear long-term trajectory can also prevent revenue from becoming degressive and diminishing gradually.39

Boosting decarbonisation

Contentions about the effectiveness of green taxes remain widespread. When asked about environmental taxation in particular as a means to tackle environmental challenges, only 15% of Europeans favour this options over others such as subsidies and tax breaks to incentivise sustainable behaviour of citizens and industry. Interestingly, relative support for environmental taxation is high in countries that have already successfully implemented some measures, such as Sweden and Germany with 20% and 19%.

Experience from forerunner countries impressively demonstrate that environmental taxation can achieve ecological objectives in a targeted and cost-efficient way. There is a rich source of evidence for the environmental benefits green taxes can yield. The carbon taxes introduced in Nordic countries have achieved astonishing cuts in greenhouse gas emissions. It is estimated that without its carbon tax introduced in 1990, Sweden’s emission levels today would be 20% higher than today’s. Meanwhile, focused, long-term-oriented environmental policy has allowed Denmark to pursue the ambitious goal of decarbonising its economy already by 2050.

Beside their direct effects green taxes also contribute to an overall better business climate for low-carbon technology as they boost eco-innovations. By inducing behaviour change and gradually discouraging environmentally distortive activities, green taxes are a key policy instrument in the decarbonisation of the European economy.

The EU risks losing its credibility with regards to international climate policy if it fails to position its member states on a transition path towards a low-carbon society. Europe is in the spotlight to deliver encompassing and comprehensive policies to account for its international responsibility. The European Commission has already highlighted the urgency to act now, stating that delaying the transition to a low-carbon economy “raises overall costs and narrows the options for effectively reducing emissions and preparing for the impacts of climate change.” Furthermore, in light of the Sustainable Development Goals recently endorsed by the UN General Assembly in 2015 to set the agenda for 2030, the EU has the opportunity to give strong signals to the international community that transition is possible by coherently adhering to its domestic environmental and climate objectives.

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C) Social dimension

Widespread concern:
“Environmental taxes are ultimately paid by the poor and contribute to social injustice.”

Another criticism which is frequently voiced against environmental taxation is that it has regressive effects on income distribution, particularly harming low-income households disproportionally. This fuels a narrative often used to juxtapose the interests of trade unions and welfare organisations against those of environmental groups and depict them as mutually exclusive and irreconcilable.

It is true that some environmental taxes, especially those that tax the consumption of basic goods and necessities such as water or electricity, are usually regressive. Yet, this issue can be oversimplified. As in the case of competitiveness, social equity and regressivity of environmental taxation depends on the exact tax type and design as well as the existence and nature of accompanying compensatory measures.

One can principally distinguish between two different types of compensation options. First, fiscal measures accompanying green taxes (for example reductions in income taxes or social security contributions) can counterbalance negative distributional effects of environmental taxation. In Sweden, for example, reduced income tax rates were used to neutralise undesired regressive effects of the green tax reform.

A second type of compensatory measures addresses undesired income distribution through direct redistribution of tax revenue via lump-sum support measures. These are usually directed at the most vulnerable groups affected by the tax. British Columbia, for instance, provided a refundable “Climate Action Tax Credit” for low-income households alongside a “Northern and Rural Homeowner” benefit support scheme. The German environmental tax reform, which comprised mixed compensatory schemes, included means-tested heating benefits which helped to alleviate the impact of energy price increases on the poorest households.

On a more aggregate level, studies have also suggested that well-targeted compensatory measures can – and do in practice – offset regressive effects on the most vulnerable social groups. The PETRE and COMETER projects used E3ME models to examine the double dividend hypothesis of environmental fiscal reforms, including the examination of energy tax impacts on income distribution. PETRE, for example stressed that at an EU aggregate level, reforms including recycling of tax revenue would yield positive real income effects for all socio-economic groups under consideration and under all scenarios.

More recently, estimates on quantifying the amount of revenue recycling which is needed to counterbalance negative distributional effects have shown that effective offsetting is possible with relatively small means. A study by Cambridge Economics modelling an energy tax reform in Spain, Poland and Hungary showed that as little as 6–8% of total energy tax package revenue sufficed for compensatory measures to offset the resulting negative effects on the poorest 20% of the population.

45 This measure however will leave out unemployed and pensioners.
47 For a list of fiscal and non-fiscal compensatory measures and examples, see annex III.
48 PETRE, short for “Resource productivity, environmental tax reform and sustainable growth in Europe” and COMETER for “Competitiveness effects of environmental tax reforms” both modelled the effects of ETR in 2007.
In addition, redistributive effects of environmental taxes differ according to the type of tax applied. They can affect the income distribution between richer and poorer households as in the case of taxation of household energy or water consumption, but can also have differentiated effects on households with similar incomes such as transport taxes. Other tax types such as air ticket taxes, especially those that additionally differentiate between class categories economy and business class, as well as car ownership taxes can even have progressive effects on income redistribution.

Finally, the economic context plays a large role as well in determining the social effect of an EFR. In times of national budget consolidation governments may seek to implement revenue-raising tax measures. Estimates suggest that in these scenarios carbon-energy tax reforms are less damaging in absolute terms than other tax measures, in particular direct income tax and VAT.51

D) Subsidiarity

Upholding the Subsidiarity Principle

Concerns about subsidiarity are central to many tax-related policy proposals on EU-level. Introducing tax-based own resources however does not entail any transfer of the power to tax to the European level. The term EU tax as it is used in this report does not relate to such a competence transfer, but rather to EU-wide minimum or uniform tax rates with revenue collection at member state level. In many areas better tax coordination can address market failures which cannot be resolved unilaterally such as the pervasive tax competition among member states. Thus, tax-based Green Own Resources can provide a distinct European added value unattainable by single EU member states.

Brexit and rising populism across Europe underlines the importance and necessity of better communication of the EU’s main policy priorities and long-term developments. The European Union is largely perceived as neglecting the social and ecological consequences of increased economic interdependence and globalisation. Policymakers need to develop a strong future vision centred on the provision of European public goods which member states alone are unable to create. In this context, tackling climate change is a defining challenge to which only the collective of European member states can provide effective solutions. This is also in line with the expectations of the majority of European citizens. In a recent Eurobarometer survey 67% of respondents indicated that they want to see more EU initiative on environment. A reformed European budget based on Green Own Resources could help to bring the EU’s deliveries closer to its citizens’ expectations.

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52 The UK government for example strongly opposed the idea of a European carbon-energy tax in the early to mid-1990s, mainly on the grounds of it being in breach of the subsidiarity principle.
2.2 Address needs and interest of target groups

Generating a broad support base for Green Own Resources requires proponents to address the various concerns of different societal groups with their own particular needs. The aim of this report is to develop a set of arguments for different Green Own Resource candidates and link them to specific target groups, addressing each one’s distinct policy priorities and concerns. The following section briefly introduces each of the five target groups referred to in the remainder of the study.

A) Green community

The green community comprises the members of European Green Parties as well as their core voters. Key values of the green community are the EU’s pathway towards sustainable development, social justice, market fairness and democratic participation. Furthermore, green parties in Europe have been traditionally supportive of European integration, making them quite receptive for the concept of Green Own Resources. Special attention should be given to underlining the environmental effectiveness of the specific instruments as well as the evidence about the effects on social equity.

B) Citizens, taxpayers

This target group comprises the non-green voter electorate. We assume that these voters put higher importance on the redistributive and economic effects of the proposed instruments rather than their environmental long-term effects. In times of austerity measures and budget consolidation, arguments in favour of Green Own Resources should focus on the revenue neutrality, cost-efficiency and the additional growth benefits of environmental taxes in comparison to alternative measures. In addition, arguments highlighting the constraints of member states and the need for European action can help to create more legitimacy of more EU intervention and integration.

C) Local councillors

This group addresses local politicians and cities with their specific interest in subsidiarity and local effects. As potential recipients of EU funding regional stakeholders are crucial to implement the EU’s sustainability agenda on the ground. The prominent role of the Covenant of Mayors underlines the influential position cities and regions maintain in realising climate and sustainability commitments. Some of the Green Own Resources discussed in this report have potentially strong effects at a local level, for example transport fuel taxes, which may increase pressure on cities to provide better and more efficient public transportation or electro-mobility. Without the support of local stakeholders and their understanding why the different political layers need to cooperate in order to implement Paris and the European Sustainability Strategy, Green Own Resources will not attain the local political support needed.

D) Industry and trade unions

This target group arguably contains the strongest opponents to Green Own Resources, at least in the case of energy, carbon and corporate taxation. Depending on the policy instrument, strong opposition can be expected from the industry sectors most affected. Support could be achieved through a focus on supporting investment trends and providing a guiding pathway for a gradual transition towards low-carbon production.

All too often critics of green taxes tend to present the interests of environmentalists and workers’ rights as irreconcilable. Key messages towards trade unions should emphasise that the regressive effects of environmental taxation are often exaggerated and can be alleviated by smart tax designs which take distributional concerns into account. In this context it is indispensable to provide examples of how environmental taxes can
in the medium-term boost quality employment and enhance economic growth.

E) Member states
Formally, the decision to reform the EU own resource system is negotiated in the Council and requires unanimity from all EU member state governments. Each instrument will reshape the composition of the budget and shift the share in national contribution, producing changes in the perception of net winners and net losers. In order to convince those countries which are likely to oppose a redistribution of own resource share to their disadvantage, the potential spill-over effects and the long-term benefits for the European economy at large need to be highlighted.
3 Communicating Green Own Resource Candidates

The remainder of this study introduces eight Green Own Resource candidates focusing on their potential in transforming the EU budget into a key instrument for enhancing sustainable development in Europe. The following table provides an overview of the candidates discussed as well as their budgetary potential.

Table 1: Overview of revenue potential of Green Own Resource candidates

<table>
<thead>
<tr>
<th></th>
<th>Annual revenue estimate (EUR)</th>
<th>Share of total EU budget</th>
<th>Share of national contributions</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>EU Carbon Tax</strong></td>
<td>28–40 billion</td>
<td>20–28%</td>
<td>23–32%</td>
</tr>
<tr>
<td><strong>BCAs</strong></td>
<td>No exact estimates available</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Energy Tax</strong></td>
<td>81 billion</td>
<td>56%</td>
<td>66%</td>
</tr>
<tr>
<td><strong>Road Fuel Tax</strong></td>
<td>40–167 billion</td>
<td>28–100%</td>
<td>32–100%</td>
</tr>
<tr>
<td><strong>EU Air Ticket Tax</strong></td>
<td>5.4 billion</td>
<td>3.8%</td>
<td>4.4%</td>
</tr>
<tr>
<td><strong>EU FTT</strong></td>
<td>30–57 billion</td>
<td>21–40%</td>
<td>24–46%</td>
</tr>
<tr>
<td><strong>EU CIT</strong></td>
<td>15 billion</td>
<td>10%</td>
<td>12%</td>
</tr>
<tr>
<td><strong>CJEU Fines</strong></td>
<td>4.5 billion</td>
<td>3.1%</td>
<td>3.6%</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>&gt; 240 billion</td>
<td>143.9 billion*</td>
<td>123.7 billion*</td>
</tr>
</tbody>
</table>

*Figures represent 100% of 2016 total EU budget and national contributions respectively.*
The table represents revenue estimates for each candidate, including lower and upper bounds in case of multiple sources\textsuperscript{54}. Figures from the 2016 total budget as well as the amount of national contributions of the same year give rough indications of the replacement potential for each candidate. Whereas estimates suggest that certain candidates will only be capable of replacing a portion of the budget, other candidates, such as the road fuel tax and the energy tax, generate enough revenue to replace a substantial part of – if not the entire – current EU budget.

The following chapter presents eight distinct Green Own Resources and develops a set of key messages that proponents might refer to when addressing specific target groups. For each instrument, a profile section briefly provides the main rationale for the instrument alongside a short overview of the respective EU action so far. This is followed by a tabular analysis of the instrument’s strengths, weaknesses, opportunities and threats relating to advantages and disadvantages inherent to the instrument as well as the broader policy context. A final section presents an inventory of arguments in favour of the instrument and its suitability as an EU own resource, grouped by the four perspectives discussed in the previous chapter.

\textsuperscript{54} For estimate sources, please see references in the respective candidate chapter.
3.1 EU Carbon Tax

3.1.1 EU Carbon Tax Profile

Definition:
Green Own Resource based on EU-wide minimum tax rate on carbon in all non-EU ETS sectors.

Key figure:
80-95% reduction on GHG emissions compared to 1990 levels as indicative goal until 2050.


Primary steering effect:
Decarbonisation of non-ETS sectors of economy representing 55% of EU GHG emissions.

Annual revenue estimate\(^5\):
EUR 28-40 billion
In % of total EU budget
20-28%
In % of national contributions
23-32%

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Background:
The Paris Agreement requires the European Union to align its greenhouse gas emission pathway with the objective of keeping the global average temperature well below 2°C. This requires enormous shifts in investment away from fossil fuel to low-carbon infrastructure. Carbon however remains incoherently priced throughout the European Union and does not provide efficient market signals for a sustainable transition towards a low-carbon economy. The Emission Trading Scheme, the EU’s flagship initiative on carbon trading and pricing, only covers 45% of all EU GHG emissions and fails to deliver a sufficiently high carbon price. Pricing mechanisms for the remaining 55% of GHG emissions are extremely patchy – only a minority of countries currently applies a domestic carbon tax. A comprehensive European-wide approach to tax carbon outside the ETS can correct these incoherencies and establish a credible and sustainable carbon price pathway until 2050 and beyond.

Rationale:
Without a credible price for carbon a market-guided transition towards a low-carbon economy in Europe is elusive. According to the European 2050 Roadmap, carbon prices of around EUR 100 to EUR 370 per tonne of CO₂ are necessary by 2050 to cut GHG emissions by at least 80–95%. This is far above the price currently generated by the EU ETS – EUR 4.02 on 7 September 2016 – covering 45% of total EU greenhouse gas emissions.

Effective carbon taxation only exists in a minority of member states. Denmark, Ireland, Finland, Sweden, France and Slovenia currently have carbon taxation in place but the tax rates differ considerably among them. A common minimum tax rate on carbon across the EU would allow for better low-carbon market signals, help member states to achieve their effort-sharing obligations and even be able – if implemented through a “tax shift” away from taxation detrimental to economic growth – to enhance overall prosperity.

The EU has highlighted its objective to decarbonise its economy by mid-century. In order to accomplish the European transition towards a low-carbon economy, the EU needs to create a sound market environment to shift the trillions of euro in investments necessary. The energy sector worldwide needs to invest EUR 12 trillion between 2015 and 2030 to fully implement the climate pledges of the Paris Agreement, representing around 40% of total global energy sector investment. Additionally, the implementation of the Sustainable Development Goals necessitates annual USD 5 to 7 trillion or EUR 4 to 6 trillion according to the UNCTAD. If the European Union fails to establish a credible and sustainable carbon price pathway until 2050, investment patterns will

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keep favouring infrastructures locked in fossil fuel and high-carbon emissions.

Clearly, the EU budget could send the strong message that decarbonisation and the transition to a low-carbon society are possible by adding a carbon tax as own resource.

**Added value as a Green Own Resource**

The lack of coherent EU-wide taxation on carbon, the distortive consequences for the Internal Market, investors and the energy sectors, and the common objective to deliver on ambitious emission targets, justify EU-wide advances in carbon tax coordination. Introducing EU-wide minimum tax rates on carbon content can level the playing field across EU member states and guarantee a consistent carbon price outside the ETS.

Carbon taxes can come in different forms. Generally, one can distinguish carbon taxes based on the emissions associated with consumption or use of fuels (destination based) and carbon taxes applying to emissions stemming from production or supply of fuels (origin based). In the past, the European Commission has proposed a form of the latter when reviewing the Energy Tax Directive in 2011. Applying only to the carbon content of fuels, a CO₂ tax of EUR 20 per tonne of carbon was estimated to generate around EUR 40 billion.⁶²

A broad-based carbon tax as discussed by Le Cacheux and Laurent (2009) would function as an equivalent to a VAT and would apply to all goods and services according to the destination principle.⁶³ Although politically and legally more challenging, such an ambitious approach could comprehensively provide better visibility of the carbon content of each good and service, which is necessary for an effective change in consumer behaviour.

**EU progress so far:**

The EU long-term targets for decarbonisation were presented in the European Commission’s 2011 Roadmap for a competitive low-carbon society. It foresaw a gradual emission reductions pathway of 40% by 2030, 60% by 2040 and 80% by 2050 (compared to the 1990 levels)⁶⁴. Unfortunately, it was not endorsed by all member states in the Council.⁶⁵ At the EU level, the Effort Sharing Decision (406/2009/EC) determines the GHG emission targets for each member state until 2020. The respective reduction targets until 2030 are currently negotiated in the Effort Sharing Regulation. Besides setting a country-specific target, they do not determine a common instrument to achieve the GHG emission reduction. In the past, the European Commission has brought forward proposals about comprehensive EU-wide carbon pricing several times already. However, concrete measures on the European level have not yet been successful. The revision of the European Energy Tax Directive, which had foreseen the inclusion of a tax base on carbon content of energy products, was ultimately withdrawn by the European Commission in 2015 after negotiations.

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stalled in the Council\textsuperscript{66}. The old Energy Tax Directive of 2003 is still in force now, although it has been characterised as being counterproductive to the Union’s energy and climate change goals and incoherent with the European system of emission permit trading\textsuperscript{67}. Carbon taxation as a potential source of EU budgetary revenue has been discussed by the European Commission as early as 1998, but has not been officially proposed yet, probably also due to the lack and delay of EU-wide carbon tax coordination so far\textsuperscript{68}.

### 3.1.2 SWOT-Analysis for EU Carbon Tax

A European-wide carbon tax can offer a number of advantages. By directly taxing carbon content or carbon emissions, the instrument would be best equipped to provide an important control mechanism for the EU greenhouse gas reduction target. There are however a number of important considerations of the tax based on national experience, in particular with regards to redistributive effects and political consensus. Without prejudice to the exact tax design, a European tax on carbon as EU own resource could have the following strengths, weaknesses, opportunities, and threats:

<table>
<thead>
<tr>
<th>STRENGTHS</th>
<th>WEAKNESSES</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Potential to tackle 55% GHG emissions outside the ETS/comprehensive implementation of ESD</td>
<td>• Possible trade-off between political consensus and environmental effectiveness (tax exemptions and tax expenditures)</td>
</tr>
<tr>
<td>• Internalise costs of carbon emissions and incentivise low-carbon patterns of consuming and producing</td>
<td>• Careful examination of redistributive effects (best design may require compensatory measures/broader tax shift)</td>
</tr>
<tr>
<td>• Revenue estimate: at least EUR 40bn</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>OPPORTUNITIES</th>
<th>THREATS</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Open policy window after Paris and the adoption of the SDGs in 2015</td>
<td>• Experience with the ETD (strong opposition to carbon component by several EU MS)</td>
</tr>
<tr>
<td>• Cross-sectoral approach with multiple spill-over effects (energy, transport, investment, infrastructure etc.)</td>
<td>• Concerns about carbon leakage</td>
</tr>
<tr>
<td>• Stepwise increase of tax rate allows for a period of gradual transition</td>
<td>• What about low-carbon leakage?</td>
</tr>
<tr>
<td>• Potential to stimulate ETS to deliver similar carbon price level</td>
<td>• Could slow down ETS reform</td>
</tr>
<tr>
<td>• Enhance decoupling of economic growth and carbon emissions</td>
<td><strong>New momentum after Paris</strong></td>
</tr>
</tbody>
</table>

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\textsuperscript{66} The 2011 proposal to revise the Energy Tax Directive suggested splitting the minimum tax rate into a carbon component fixed at EUR 20 per tonne of CO\textsubscript{2} and an energy component i.e. on the actual energy that a product generates measured in Gigajoules (GJ). European Commission (2011e). Revision of the EU Energy Tax Directive – technical press briefing. Presentation by Rolf Diemer, DG Taxation and Customs Union. Accessed 01.10.2016.


### Key messages for EU Carbon Tax

**Table 2: Key messages per target group supporting an EU carbon tax as a Green Own Resource**

<table>
<thead>
<tr>
<th>EU Carbon Tax</th>
<th>ECONOMY</th>
<th>SUSTAINABILITY</th>
<th>SOCIAL</th>
<th>EUROPE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Green Community</td>
<td>● Decarbonisation&lt;br&gt;● Carbon Bubble&lt;br&gt;● Low-carbon leakage</td>
<td>● Decarbonisation&lt;br&gt;● Non-ETS GHGe reductions&lt;br&gt;● Policy coherence</td>
<td>● Decarbonisation&lt;br&gt;● Tax shift</td>
<td>● Decarbonisation&lt;br&gt;● Effort-Sharing</td>
</tr>
<tr>
<td>Citizens</td>
<td>● Carbon Bubble</td>
<td>● Policy coherence</td>
<td>● Tax shift</td>
<td>● EU added value</td>
</tr>
<tr>
<td>Local Councillors</td>
<td>● Carbon Bubble&lt;br&gt;● Low-carbon leakage</td>
<td>● Policy coherence</td>
<td>● Tax shift</td>
<td>● Effort-Sharing</td>
</tr>
<tr>
<td>Industry</td>
<td>● Decarbonisation&lt;br&gt;● Carbon Bubble&lt;br&gt;● Low-carbon technology&lt;br&gt;● Low-carbon leakage</td>
<td>● Decarbonisation&lt;br&gt;● Non-ETS GHGe reductions</td>
<td>● Decarbonisation&lt;br&gt;● Tax shift</td>
<td>● Decarbonisation&lt;br&gt;● EU added value&lt;br&gt;● Effort-Sharing</td>
</tr>
<tr>
<td>Member states</td>
<td>● Decarbonisation&lt;br&gt;● Carbon bubble&lt;br&gt;● Low-carbon technology&lt;br&gt;● Low-carbon leakage</td>
<td>● Decarbonisation&lt;br&gt;● Non-ETS GHGe reductions&lt;br&gt;● Policy coherence</td>
<td>● Decarbonisation&lt;br&gt;● Tax shift</td>
<td>● Decarbonisation&lt;br&gt;● EU added value&lt;br&gt;● Effort-Sharing</td>
</tr>
</tbody>
</table>

**ECONOMY**

**Decarbonisation:** “A European carbon tax can stimulate the enormous shift in investment needed to make the transition towards a low-carbon economy possible.”

**Target Groups:** Green community, industry, member states

Carbon taxation is the most effective instrument capable of translating the pledges to achieve a coherent pricing of carbon into action. The EU has recently ratified the Paris Agreement which necessitates Europe enhancing its efforts to decarbonise its economy. EU Green Own Resources stemming from a European carbon tax can effectively and coherently deliver the carbon price needed for a predictable and controlled transition towards a low-carbon economy.

**Carbon Bubble:** “Early and effective carbon pricing can help shift the billions away from carbon-intensive assets, reducing the risk of a carbon bubble.”

**Target Groups:** Green community, citizens, local councillors, industry, member states

Europe needs to make sure that its economy and finances are on a sustainable path and align to the Paris Agreement objective of making financial flows consistent with a trajectory towards low greenhouse gas emissions and climate-resilient development. Currently, however, European financial institutions and service providers are still highly exposed to fossil fuel assets. EU pension funds currently hold approximately EUR 260 to 330 billion in these soon-to-be overvalued assets, banks hold EUR 460 to 480 billion and insurance companies around EUR 300 to 400 billion, leading to a total exposure of European financial
institutions exceeding EUR 1 trillion. Early implementation of an all-economy carbon price through a functioning ETS and a coherent EU carbon tax can avert a scenario in which Europe has to decarbonise abruptly and rapidly, and prevent the carbon bubble from bursting.

Low-carbon technology: “Effective carbon pricing is necessary to provide certainty for investors, enhance the efficient use of resources and make sure that the EU becomes a competitive world leader in low-carbon technology.”

Target Groups: Industry, member states

Drawing on the concerns about Europe’s international competitiveness usually used to oppose environmental taxation, it is worth posing the question of which factors will determine international competitiveness in the next decades. Emphasising the role of the European Union as a global economic actor, it is important to stress that we have already entered into a competition for the future global lead in low-carbon technology. Thus, the earlier Europe achieves the establishment of a credible carbon price able to guide a pathway towards absolute decarbonisation, the earlier Europe will be able to decouple economic growth from carbon emissions and become a leader in low-carbon technologies.

Low-carbon leakage: “Experience shows that carbon pricing instruments, when smartly implemented, can actually enhance rather than harm competitiveness.”


SUSTAINABILITY

Non-ETS GHGe reduction: “An EU-wide carbon tax effectively reduces GHG emissions of non-ETS sectors.”

**Target Groups:** Green community, industry, member states

Carbon taxation directly applies to sectors outside the EU ETS, addressing households, transport, small business and agriculture. Non-ETS emissions account for 55% of total GHG emissions in the EU. The withdrawn Impact Assessment of the Energy Tax Directive estimates that a gradual EU carbon tax of EUR 22 per tCO\(_2\) for the period 2013–2020 and EUR 30 per tCO\(_2\) for the period 2021–2030 would reduce CO\(_2\) emissions in the EU by 3.45%-75. An EU own resource based on carbon taxation can support the EU in paving the way for its long-term emission reduction goals.

**Policy coherence:** “Carbon taxation can restore coherence in the EU’s climate and environmental policy.”

**Target Groups:** Green community, citizens, local councillors, industry, member states

European climate policy is far from coherent. The EU’s flagship project, the European Emission Trading Scheme is paralysed by an oversupply of allowances as well as political reluctance to reform and has so far not delivered a sufficient carbon price. At the same time, European and world leaders pledge their commitment towards curbing the global temperature rise due to climate change, but fail to comprehensively phase out environmentally harmful subsidies\(^{76}\). Achieving a constant carbon price in non-ETS sectors can give guiding signals to investors and consumers and rebuild policy coherence in the EU’s climate instruments.

SOCIAL

**Tax shift:** “A European Carbon Tax as part of a wider Environmental Tax Reform can bring economic and environmental benefits without harming low-income households.”

**Target Groups:** Green community, citizens, local councillors, industry, member states

The redistributive effects of a European carbon tax largely depend on whether and how member states decide to use tax recycling in order to shield low-income segments from undesired regressive effects. Such compensatory measures range from labour tax reductions that alleviate the overall tax burden on income to lump sum payments towards specific households. When Sweden introduced its carbon tax in 1991 for example, it was accompanied by a broader tax shift reducing non-wage labour costs. There is almost no evidence of regressive effects of environmental taxes in Sweden, with only some being reported from increases in road fuel taxation.

EUROPE

**EU added value:** “In an integrated European market, unilateral carbon tax initiatives are always inferior to EU-wide tax application.”

**Target Groups:** Citizens, member states

Carbon emissions are a transnational challenge. Emissions have negative consequences for all European countries and do not stop at the national border. Carbon taxation is based on a mobile tax base, raising the potential of carbon leakage and subsequent tax ineffectiveness. The European Union needs to take a leading role in the mitigation

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76 Exact estimations vary depending on the definition of what constitutes a subsidy and range from EUR 34 billion to more than EUR 200 billion per year, depending on the benchmark. European Commission (2014b). Enhancing comparability of data on estimated budgetary support and tax expenditures for fossil fuels. Final Report.
of climate change, and developing an adequate price of carbon is a core project of that mission. Europe has committed to the Paris Agreement and the implementation of the Sustainable Development Goals.

**Effort-Sharing:** “A European carbon tax can support the member states in achieving their obligations under the Effort-Sharing Decision.”

**Target Groups:** Green community, local councillors, member states

Currently, the EU only determines the national reduction targets towards the Europe 2020 objectives under the Effort-Sharing Decision (406/2009/EC). A binding framework for the period 2021 until 2030 is currently negotiated. The proposal envisages however increasing member states’ flexibility in artificially offsetting shortfalls in GHGe reductions, inter alia by covering some non-ETS emissions with emission allowances or permits from the land use, land use change, and forestry (LULUCF) sector. Estimates show that these loopholes in the current post-2020 effort-sharing design could in a worst case scenario lead to an increase of GHG emissions of 2.3 billion tonnes of CO₂ by 2030. A common EU carbon tax could help the EU to meet its Paris pledge and allow member states a coordinated trajectory to achieve their binding national targets without resorting to distortive flexibility mechanisms.

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77 In July 2016, the European Commission proposed a binding post-2020 framework to steer member states’ emission reductions, the “Effort-Sharing Regulation”.

3.2 Border Carbon Adjustments

3.2.1 Border Carbon Adjustments Profile

Definition:
Green Own Resource based on obligation to purchase ETS allowances for importers of energy-intensive goods offsetting the difference in carbon pricing inside and outside the EU.

Key figure:
2.1 billion emission allowance surplus preventing the generation of a credible carbon price.


Primary steering effect:
Strengthening effectiveness of the EU ETS and reducing the risk of carbon leakage.

Annual revenue estimate:
No exact estimates available – highly depends on ETS carbon price development and the occurrence of trade retaliation.
Background:
Opponents to comprehensive environmental regulation usually argue that there is an inherent trade-off between environmental protection on the one side and international competitiveness on the other. Rather than looking at the medium- and long term resource and cost benefits for the entire economy, environmental protection is often portrayed to increase production costs on a micro level, burdening local industries and driving them out of the EU, instead of providing a business case and a competitive advantage for EU’s industry.

By relocating production to countries with more lenient environmental legislation, overall emissions could rise, a phenomenon often referred to as ‘carbon leakage’. These contentions were the main reason behind the massive free allocation of allowance permits under the EU Emission Trading Scheme (EU ETS). This oversupply is often cited the main reason why the ETS has not delivered a sufficiently high price for carbon yet.

Rationale:
Border carbon adjustments (BCAs) address these concerns directly. Usually discussed as a tax to imports or as a rebate to exports, they can also be employed as an obligation for importers to purchase ETS allowances. They balance the cost difference between domestic and foreign, mainly energy-intensive goods caused by different carbon pricing standards, therefore maintaining price competitiveness of domestic products and reducing the risk of carbon leakage.

Smartly designed BCAs can be compatible with WTO rules, create incentives for businesses and countries to invest in lower-emissions technology and substitute the free allocation of allowances under the EU ETS which is currently preventing any reasonably carbon price to unfold.79

Value added as a Green Own Resource
The revenue from BCAs based on emission allowance purchases could be derived from imports of energy-intensive goods to the Union. Since the adjustments would be directly linked to the EU ETS and their main objective is the safeguarding of its proper functioning while maintaining high EU environmental standards, its revenue allocation to the EU budget as a Green Own Resource can be justified.

EU progress so far:
BCAs are usually discussed as a desirable complement to intra-EU carbon pricing mechanisms. Under the current EU ETS regime, energy- and carbon intensive industry sectors are given a high share of free allowances to bolster challenges to their competitiveness.80 At the beginning of the current trading phase in 2013, the manufacturing industry received 80% of its allowances for free.81 This has led to an oversupply of allowances to amount to 2.1 billion allowances.82 This oversupply of allowances has kept the EU carbon price too low and explains why there is still no existing evidence of carbon leakage.83 On the contrary, the current inconsistencies of EU climate policy lead to what some have labelled a “low carbon leakage”

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80 The industries eligible to receive a higher share of free allowances in the current trading phase are those identified to be subjected to a significant risk of carbon leakage and are included in a Commission Decision listing the relevant sectors and subsectors.
referring to the emigration of low carbon technology to other world regions. But with the ratification of the Paris Agreement in 2016, a rise in the price of carbon and subsequent pressure on high-emitting industry sectors is a probable option. In such a scenario BCAs would be a desirable option to maintain the carbon price and safeguard competitiveness at the same time.

Although there are currently no BCAs in place, estimations on the potential effects have shown that sectoral BCAs focusing on emission-intensive trade exposed (EITE) sectors such as the aluminium industry could yield higher carbon prices, investment, output and employment while a gradual expansion to other sectors could close the remaining loopholes of current carbon pricing.

3.2.2 SWOT-Analysis for Border Carbon Adjustments

A Green Own Resource based on BCAs would be a precedent in international trade. BCAs may have been recurrent topic of political discussion, but have not been adopted so far. This explains the lack of revenue estimates and experience-based effects on trade. In Europe, the past reluctance to implement BCAs stems partially from national governments’ priorities on economic recovery during the economic crisis. It is crucial to carefully weigh reservations and implications about trade retaliation against BCAs’ stabilising effects on the allowance-market.

Although there are currently no BCAs in place, estimations on the potential effects have shown that sectoral BCAs focusing on emission-intensive trade exposed (EITE) sectors such as the aluminium industry could yield higher carbon prices, investment, output and employment while a gradual expansion to other sectors could close the remaining loopholes of current carbon pricing.

<table>
<thead>
<tr>
<th>STRENGTHS</th>
<th>WEAKNESSES</th>
</tr>
</thead>
<tbody>
<tr>
<td>▪ Maintain price competitiveness of EU products with sophisticated environmental standards</td>
<td>▪ Second best option in lack of global approach (WTO)</td>
</tr>
<tr>
<td>▪ Compatible with WTO rules</td>
<td>▪ Entails additional administrative costs</td>
</tr>
<tr>
<td>▪ Incentivises domestic and international investments in low-carbon production</td>
<td>▪ Could lead to trade retaliation</td>
</tr>
<tr>
<td>▪ Support EU ETS reform process as well as coherent EU-wide carbon pricing</td>
<td></td>
</tr>
<tr>
<td>▪ Creates jobs in the EU instead of “exporting” them</td>
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<thead>
<tr>
<th>OPPORTUNITIES</th>
<th>THREATS</th>
</tr>
</thead>
<tbody>
<tr>
<td>▪ Table environmental and sustainable aspects to international trade considerations</td>
<td>▪ Danger to develop into a protectionist tool</td>
</tr>
<tr>
<td>▪ ETS may require post-reform support (free allowances will be backloaded, not deleted)</td>
<td>▪ Focus on climate mitigation rationale crucial</td>
</tr>
<tr>
<td></td>
<td>▪ Resistance from WTO members</td>
</tr>
<tr>
<td></td>
<td>▪ Compatibility with WTO rules needs to be stressed</td>
</tr>
</tbody>
</table>

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3.2.3 Key messages for Border Carbon Adjustments

Table 3: Key messages per target group supporting BCAs as a Green Own Resource

<table>
<thead>
<tr>
<th>Border Carbon Adjustments</th>
<th>ECONOMY</th>
<th>SUSTAINABILITY</th>
<th>SOCIAL</th>
<th>EUROPE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Green Community</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Support EU ETS</td>
<td>• Making trade greener and fairer</td>
<td></td>
<td>• Effort-Sharing</td>
</tr>
<tr>
<td></td>
<td>• International competitiveness</td>
<td></td>
<td></td>
<td>• Paris-consistent global trade</td>
</tr>
<tr>
<td>Citizens</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>• International competitiveness</td>
<td></td>
<td></td>
<td>• Making trade greener and fairer</td>
</tr>
<tr>
<td>Local Councillors</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>• International competitiveness</td>
<td>• Support EU ETS</td>
<td>• Making trade greener and fairer</td>
<td></td>
</tr>
<tr>
<td>Industry</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>• International competitiveness</td>
<td>• Support EU ETS</td>
<td>• Making trade greener and fairer</td>
<td>• Effort-Sharing</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Level the global playing field</td>
<td></td>
<td>• Paris-consistent global trade</td>
</tr>
<tr>
<td>Member states</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>• International competitiveness</td>
<td>• Support EU ETS</td>
<td>• Making trade greener and fairer</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Level the global playing field</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**ECONOMY**

International competitiveness: “EU own resources based on BCAs can remedy concerns about carbon leakage and can safeguard international competitiveness.”

**Target Groups: Citizens, local councillors, industry, member states**

Concerns about the effects on competitiveness have often prevented the introduction of stringent and pervasive environmental and carbon pricing instruments. This is why the EU has granted installations of industries with a ‘significant risk’ of carbon leakage free allowances under the current ETS trading phase until 2020. The resulting oversupply of allowances and the stagnant ETS reform have inhibited the price of allowances from rising to sufficient levels. BCAs. This may explain why there is currently little to no evidence of carbon leakage occurring.

Given the increasing necessity to improve carbon pricing in the Union, this may well change. In the long-term and preferably as of 2020, BCAs are a viable alternative to the free allocation of allowances. They would retain the function of free allowance allocation in preventing carbon leakage while at the same time eliminating the allowance oversupply and allowing the ETS to generate a more credible carbon price, hence, implementing the “polluter pays” principle.

**SUSTAINABILITY**

Support EU ETS: “Border carbon adjustments effectively support existing carbon pricing mechanisms.”

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86 Indicative estimates show that both in general as well as partial equilibrium models, BCAs could successfully reduce leakage rates, even if most studies are based on current mitigation rates and a generally low carbon price level. Vivid Economics (2012). Carbon taxation and fiscal consolidation: the potential of carbon pricing to reduce Europe’s fiscal deficits. Report by Green Budget Europe. Accessed 01.10.2016.
**Target Groups:** Green community, local councillors, industry, member states

BCAs can help alleviating reservations against instruments applying the polluter pays principle. These reservations have led to a number of distortive exceptions and deals with specific industry branches in the past. At the beginning of the current trading phase of the EU ETS in 2013, for example, the manufacturing industry received 80% of its allowances for free\(^87\) leading to an oversupply of allowances estimated to amount to 2.1 billion allowances\(^88\). This oversupply of allowances has kept the EU carbon price within ETS sectors far below any rate that would be necessary to provide credible and sufficient market signals to steer investments towards low-carbon technology\(^89\).

Indicative estimations on the potential carbon price effects of BCAs have shown that sectoral BCAs focusing on emission-intensive trade exposed (EITE) sectors such as the aluminium industry could yield higher carbon prices, investment, output and employment while a gradual expansion to other sectors could close the remaining loopholes of current carbon pricing.

**Level the global playing field:** “BCAs can induce and stimulate carbon mitigation efforts within the EU and abroad.”

**Target Groups:** Green community, industry, member states

By imposing a tax on the associated emissions of imported products BCAs also create incentives for producers in EU trading partner countries to shift towards low-carbon or energy efficient means of producing in order to keep costs for access to the European market as low as possible. For countries for which the EU is an important export market, BCAs can create economic incentives to enhance domestic environmental regulations.

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**SOCIAL**

**Making trade greener and fairer:** “Smart BCAs can apply the polluter pays principle to EU trade while taking into account the economic context of its trading partners.”

**Target Groups:** Green community, citizens, local councillors, member states

By balancing the difference in product prices stemming from different carbon pricing standards, lower standard products can only enter the Single Market if the difference is paid in form of a BCA. Replacing the free allowances inside the EU ETS, BCAs could function as an alternative remedy to carbon leakage by imposing charges to foreign products balancing out their price advantage stemming from lower environmental standards. This would not only generate potential revenue within the EU, but could also create jobs as the import of cheaper goods becomes less lucrative. “Smart BCAs” can reflect principle of common but differentiated responsibility\(^90\). They are calibrated to a trading partner’s income level and take into account capacity to mitigate emissions. They also benchmark against other countries, comparing their carbon prices.

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**EUROPE**

**Effort-Sharing:** “BCAs complementing EU climate action can facilitate ambitious national reduction pathways.”

**Target Groups:** Green community, member states

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Concerns about competitiveness are reoccurring obstacles for the adoption of ambitious and binding national climate targets as the recent adoption of the national objectives in the Effort-Sharing Regulation underlines. By reducing the likeliness of carbon leakage, BCAs can improve member states’ negotiation position in favour of adopting comprehensive and profound climate change mitigation policy.

**Paris-consistent global trade**: “Post-Paris global trade makes a good case for BCAs.”

**Focus Target Groups**: Green community, member states

BCAs are a desirable complement in times of differentiated global action on climate change mitigation. The Paris Agreement did create a common global target of keeping temperature rise well below 2°C in this century, but the way to get there, hence individual climate and environmental standards, will be far from uniform. BCAs can address this diversification of international carbon standards and guarantee that European products retain their price competitiveness throughout uneven carbon pricing regimes adopted in different regions in the world. In December 2015, the European Parliament did already consider the adoption of WTO-compatible BCAs in such a scenario.

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91 The lack in ambition of the EU’s national 2030 targets will force member states to abruptly raise their reduction efforts in post-2030. EEB (2016). Commission proposal sticks with outdated climate targets. Press release from 20 July 2016.

92 The diversification of climate standards across the world is likely to increase over time, given the need for countries to considerably boost their ambition in the years to come. The current pledges to the Paris Agreement (INDCs), if implemented successfully, will keep the global temperature rise only below 3.5°C missing the 2°C target by 1.5° with a larger than 66 percent chance according to the Emission Gap Report of the UNEP. UNEP (2015). The Emissions Gap Report 2015. A UNEP Synthesis Report.

3.3 Energy Tax

3.3.1 Energy Tax Profile

Definition:
Green Own Resource drawn from common progressive minimum tax rates on energy products according to their energy content.

![Key figure: Share of renewable energy in gross final energy consumption, by country, 2005 and 2014.](image)

(*Iceland and Norway have adopted mandatory targets under Directive 2009/28/EC (see EEA Agreement, Annex IV).)


Primary steering effect:
Strengthening energy savings and energy efficiency efforts and promoting the use of renewables.

Annual revenue estimate[^54]:

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Background:
Energy taxes provide the largest source of environmental tax revenue in the EU. Currently, member states adopt nationally determined rates to the volume of energy consumed which must respect the European minimum rates of the Energy Tax Directive (Council Directive 2003/96/EC). Yet, these rates ignore the diversity in energy contents of different energy carriers and are set at a generally low level. Furthermore, they do not reflect the carbon content of a fuel. Thus, tax rates vary strongly among member states and are not used to promote specific forms or sources of energy, in particular renewables. Against the backdrop of the ratification of the Paris Agreement and the EU’s efforts to integrate the energy market under the Energy Union initiative, energy-tax based Green Own Resources can provide the ground for a better, more efficient and more sustainable energy taxation throughout the EU.

Rationale:
The Energy Tax Directive provides the taxation of energy sources solely based on the volume consumed. This puts renewables at a disadvantage with fossil fuel energy products. An EU own resource based on energy taxation which differentiates energy content would promote the use of renewable energy and encourage energy efficiency at the same time. At the moment, the most polluting energy sources like coal are the least taxed. On the contrary, biofuels – due to their relatively low energy content in comparison to fossil fuels – are amongst the most heavily taxed energy sources. This constitutes a major inconsistency with the EU’s commitment to increase the share of renewable energies and to deliver affordable, sustainable and efficient energy supply.

The EU has repeatedly underlined its determination, in particular in the context of the launch of the Energy Union, to becoming “the world leader in renewable energy, the global hub for developing the next generation of technically advanced and competitive renewable energies”95. Green energy tax-based own resources can provide the necessary fiscal framework to achieve this European energy transition.

Value added as a Green Own Resource
A European energy market based on renewables requires a paradigm shift in the way energy is currently taxed. EU own resources based on sustainable energy taxes could enhance European wide coordination of energy tax rates and provide the basis for adjusting the EU minimum rates in a way that incentivises the use of renewables. This adjustment should entail the differentiation of minimum energy tax rates based on energy content rather than taxing volume which currently puts low energy content carriers, especially biofuels at a systemic disadvantage. The timing of the EU reform process coinciding with the ratification of the Paris Agreement and the launch of the Energy Union constitutes a crucial momentum for addressing the prevailing inconsistencies of the Energy Tax Directive and for delivering better, future-oriented energy taxation.

EU progress so far:
After a reform proposal by the EU Commission in 2011 aiming at introducing a tax rate based on both, the energy and the carbon content of an energy carrier, the revision of the Energy Tax Directive was blocked in the Council. The EU Commission dropped the proposal in 2015, since Council negotiations had resulted in fully denaturing the substance of the Commission proposal, according to the official reason of withdrawal96. In other words: the

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counterproductive provisions of the 2003 Directive still apply. They risk however to be in conflict with the EU’s medium- and long term climate and energy objectives as they are more suitable for a fossil fuel-powered economy. In spite of the persistence of this outdated tax structure, the EU has committed to increase the share of renewable energies to 27% by 2030 while the European Council has endorsed the indicative target to achieve 27% increase in energy efficiency by 2030\(^97\). At the same time, the Paris Agreement and the Sustainable Development Goals add support to a European energy transition narrative. The sub-targets of SDG 7 explicitly stress the employment of renewable energy and enhancement of energy efficiency by 2030\(^98\).

### 3.3.2 SWOT-Analysis for Energy Tax

Some obvious advantages of energy taxes as an own resource base such as their prevalence in all EU member states and their stable and ample revenue streams need to be weighed against some required additional efforts to reduce their regressive distributional effects. One option to remedy these undesired consequences is to recycle potential additional tax revenue by reducing national employers’ social security contributions. According to the European Commission’s Impact Assessment of an EU energy tax based on energy content, real income would increase in all socio-economic groups and income quintiles fairly proportionally, assuming that tax revenues are entirely recycled\(^99\).

<table>
<thead>
<tr>
<th>STRENGTHS</th>
<th>WEAKNESSES</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Energy taxes are a sufficient and stable source of income</td>
<td>- National tax recycling needed to balance distributional effects</td>
</tr>
<tr>
<td>- Increase energy efficiency and energy saving, improve energy security and diversity and promote renewable energy</td>
<td>- Minimum rate adjustment necessary to differentiate energy product based on energy content</td>
</tr>
<tr>
<td>- Build upon existing collection structures in all member states thus inexpensive to administer</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>OPPORTUNITIES</th>
<th>THREATS</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Energy Union provides further justification of making energy tax coordination more efficient</td>
<td>- Sensitive to MS national coffers as it is the largest source of environmental tax income</td>
</tr>
<tr>
<td>- Future tightening of energy-saving targets, in line with SDG agenda</td>
<td>- Recent experience of failed ETD revision</td>
</tr>
</tbody>
</table>

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### 3.3.3 Key messages for Energy Tax

<table>
<thead>
<tr>
<th>Energy Tax</th>
<th>ECONOMY</th>
<th>SUSTAINABILITY</th>
<th>SOCIAL</th>
<th>EUROPE</th>
</tr>
</thead>
</table>
| Green Community | • Affordable energy transition  
• Fairer energy market | • A Paris-consistent path for renewables | • Tax recycling for progressive distribution  
• Integrated budget for energy transition | • Towards a Green Energy Union |
| Citizens | • Affordable energy transition  
• Stability and Sufficiency  
• Towards more energy independence | | • Tax recycling for progressive distribution  
• Integrated budget for energy transition | |
| Local Councillors | • Affordable energy transition  
• Fairer energy market  
• Towards more energy independence | | | • Integrated budget for energy transition |
| Industry | • Affordable energy transition  
• Fairer energy market  
• Towards more energy independence | • A Paris-consistent path for renewables | • Integrated budget for energy transition | |
| Member states | • Affordable energy transition  
• Stability and Sufficiency  
• Towards more energy independence | • A Paris-consistent path for renewables | • Tax recycling for progressive distribution  
• Integrated budget for energy transition | • Towards a Green Energy Union |

#### ECONOMY

**Affordable energy transition:** “Energy tax-based EU own resources can support a gradual cost-efficient European energy transition.”

**Target Groups:** *Green community, citizens, Industry, local councillors, member states*

The Paris Agreement has set the timeline for Europe’s decarbonisation. The EU and its member states need to develop ambitious and swift solutions to achieve a timely transition to sustainable, affordable and low-carbon energy supply. If neither Carbon Capture and Storage (CCS) nor nuclear energy develop the economic and technological capacities, as well as the public acceptance, rapidly enough to replace fossil fuel power, which is likely to be the case given the time pressure and the wide-spread reservations about CCS and nuclear power, renewables will power the main share of Europe’s energy mix. This requires large investment shifts to renewables and more flexible and interconnected energy infrastructure.

However, the European Systemic Risk Board has stressed that although renewables are currently the fastest growing energy source category, “roughly 70% of new energy investment is related
Weyzig et al. (2014) have estimated the asset portfolio of European financial institutions in fossil fuel firms to exceed EUR 1 trillion with potential losses ranging from EUR 350-400 billion\textsuperscript{101}. Delaying the inevitable adjustments in favour of renewables is likely to lead to a belated and abrupt transition which will have exponential costs for the European economy.

**Fairer energy market:** “A common EU own resource on energy taxes can help eliminating the fiscal disadvantage of renewables and make use of the full growth potential of the renewable energy technology sector.”

**Target Groups:** *Green community, local councillors, industry*

The enduring existence of fossil fuel subsidies, estimates range between EUR 34 billion and more than EUR 200 billion per year in the EU\textsuperscript{102}, the generous tax expenditures and exemptions for energy-intensive industries together with EU minimum tax rates which do not differentiate between renewables and non-renewables create severe distortions in the energy market which hamper the renewable sector to develop its full potential. Despite these structural difficulties, in 2014, European renewable energy businesses already employ over a million people throughout the EU and yielded a combined annual turnover of EUR 129 billion\textsuperscript{103}.

**Stability and Sufficiency:** “Green Own Resources based on energy taxes are a desirable option due to their stable and sufficient revenue generation.”

**Target Groups:** *citizens, member states*

Energy tax revenue is one of the most stable income sources among environmental taxation as energy is a necessity with a low price elasticity of demand. At the same time, it is a rich source of government revenue. Energy taxes make up 77% of total environmental taxation across the European Union. With total revenue from environmental taxes in 2013 amounting to over EUR 343 billion, energy taxes would therefore generate roughly

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EUR 263 billion annually, sufficient resources to cover the entire annual EU budget or to provide for a substantial share of own resources co-financing. In its 2004 report on the operation of the own resources system, the European Commission stated that “EU rates below half of the minimum rates would be enough to finance half of the current EU budget” making energy taxation a very attractive candidate for future own resources. The HLGOR estimates own resource volume from energy taxes to amount to at least EUR 81 billion.

Towards more energy independence: “The further expansion of renewable energy production reduces Europe’s energy dependency.”

**Target Groups:** Citizens, local councillors, industry, member states

Since 2004, the EU imports more than half of the energy it consumes. Over twenty five years, energy dependency has increased by almost 10%. Currently, almost 90% of crude oil as well as 66% of natural gas is imported, notably from Russia, adding to concerns about the EU’s long-term energy security. Besides intensifying domestic energy production in general, the expansion of alternative energy sources, especially renewables can in the long-term reduce Europe’s vulnerability to external energy supply shortages. In its Communication on European Energy Security, the European Commission explicitly stresses the role energy taxes could play in overcoming the EU’s excessive energy dependence.

**SUSTAINABILITY**

A Paris-consistent path for renewables: “Smarter taxation of energy can bring renewables’ growth rate in line with the EU’s long-term decarbonisation target.”

**Target Groups:** Green community, industry, member states

Renewables currently account for around a quarter of total energy produced in Europe. 43.7% of all energy produced still comes from fossil fuel, but the trend of renewables is rising (see figure 10). Currently, the EU is on track to achieve its 20% renewables target until 2020. This is with the exception of the transport sector for which the target of 10% renewables is likely to be missed. According to the Commission’s evaluation, uncertainty about the environmental implications of certain biofuels, an ambiguity which better taxation could have alleviated, have let to the stagnation of political action in this area. Unfortunately, the EU’s post-2020 renewable trajectory reflects a similar political fatigue. The 2030 energy and climate targets foresee a mere increase of renewable energy share of final energy consumption by 27% compared to 1990 levels. This entails an unambitious annual growth rate of 1-1.5%, far below the growth rates needed to prepare the EU for a sustainable pathway towards decarbonisation by mid-century.
coordinated energy tax rates consistent with the Paris objective can create a level playing field promoting the deployment of renewables across the EU. Such an EU-wide approach is a desirable remedy for the lack of binding national targets for renewables under the EU 2030 agenda\textsuperscript{113}. 

![Figure 7: Gross inland consumption, EU-28, 1990–2014 in percentage share of total consumption](source)

\textbf{SOCIAL}

\textbf{Tax recycling for progressive distribution:} “Smart tax recycling can effectively offset undesired distributional effects of additional tax revenue.”

\textbf{Target Groups:} Green community, citizens, member states

As mentioned above, energy is a necessity. This makes EU own resources based on energy taxes a stable and sufficient revenue source, but has unwelcome consequences for income redistribution if tax increases are not accompanied by smart complementary measures. Since low-income earners on average pay a higher share of their income on necessities, a price increase in taxes on these goods results in a higher proportional burden for these income groups. Tax recycling can however offset these effects. The European Commission’s Impact Assessment estimates that an EU energy tax based on energy content can, if tax revenue would be recycled to lower employers’ social security contributions, increase real disposable income in all socio-economic groups fairly proportionally\textsuperscript{114}. All member states have a compensation scheme in

\textsuperscript{113} In contrast to the 2030 target which only establishes a 27% renewables target bidding at the EU level, the 2020 targets were broken down in national targets and trajectories governed by the Renewable Energy Directive (2009/28/EC).

\textsuperscript{114} Whereas increases in energy taxes of 10% without any compensatory measure would have a regressive effect, reducing real income for the poorest population quintile by 0.69 and the wealthiest by 0.43, the lowest socio-economic group gains 0.1 and the richest 0.08 when all tax revenue is recycled. European Commission (2012a). Impact Assessment accompanying Regulation (EU) No 1031/2010 determine the volumes of greenhouse gas emission allowances to be auctioned in 2013-2020. \textit{SWD/2014/50}. Accessed on 01.10.2016.
place which could be used also for increased energy taxes.

**Integrated budget for energy transition:** “Energy tax-based own resources allow for an integrated vision of the EU’s revenue, expenditure and political priorities.”

**Target Groups:** Green community, citizens, local councillors, industry, member states

The promotion of energy efficiency and renewable energy through the EU budget’s revenue side complements important funds among EU expenditure some of which could also be reinforced through the choice of energy-taxes as EU own resources. This is particularly true for the European Energy Efficiency Fund, the Connecting Europe Facility and the European Energy Programme for Recovery. The EU should encourage regions experiencing higher infrastructural challenges in meeting the demands for an interconnected renewable energy market through well targeted funding that ensures a fair burden sharing of the European energy transition.

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**EUROPE**

**Towards a Green Energy Union:** “Green Own Resources based on energy taxes can achieve the common good of a Green Energy Union.”

**Target Groups:** Green community, member states

Higher energy independence, clean, smart and inexhaustible energy affordable for everyone and the collective decarbonisation are meaningful and enduring public goods a future European budget should show capable of providing to EU citizens. Building its budget on energy-based own resources which can promote sustainable energy supply through better market signals, the EU can show that it is still a frontrunner in energy technology, ambitious climate policy and sustainable development.
3.4 Road Fuel Tax

3.4.1 Road Fuel Tax Profile

Definition:
Own Resource based on CO₂-neutral minimum tax rates for petrol and diesel.

Key figure: Sector-specific GHGe between 1990 and 2014.

<table>
<thead>
<tr>
<th>Source category</th>
<th>Million tonnes (CO₂-equivalent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Road transportation (CO₂ from 1.A.3.b)</td>
<td>124</td>
</tr>
<tr>
<td>Refrigeration and air conditioning (HFCs from 2.F.1)</td>
<td>99</td>
</tr>
<tr>
<td>Aluminium production (PFCs from 2.C.3)</td>
<td>– 20</td>
</tr>
<tr>
<td>Fugitive emissions from natural gas (CH from 1.B.2.b)</td>
<td>– 20</td>
</tr>
<tr>
<td>Enteric fermentation: dairy cattle (CH from 3.A.1)</td>
<td>– 21</td>
</tr>
<tr>
<td>Agricultural soils: direct N₂O emissions from managed soils (N₂O from 3.D.1)</td>
<td>– 25</td>
</tr>
<tr>
<td>Cement production (CO₂ from 2.A.1)</td>
<td>– 28</td>
</tr>
<tr>
<td>Fluorochemical production (HFCs from 2.B.9)</td>
<td>– 29</td>
</tr>
<tr>
<td>Nitric acid production (N₂O from 2.B.2)</td>
<td>– 45</td>
</tr>
<tr>
<td>Enteric fermentation: cattle (CH from 3.A.1)</td>
<td>– 47</td>
</tr>
<tr>
<td>Commercial/institutional (CO₂ from 1.A.4.a)</td>
<td>– 56</td>
</tr>
<tr>
<td>Adipic acid production (N₂O from 2.B.3)</td>
<td>– 57</td>
</tr>
<tr>
<td>Manufacture of solid fuels and other energy industries (CO₂ from 1.A.1.c)</td>
<td>– 62</td>
</tr>
<tr>
<td>Coal mining and handling (CH from 1.B.1.a)</td>
<td>– 75</td>
</tr>
<tr>
<td>Managed waste disposal sites (CH from 5.A.1)</td>
<td>– 76</td>
</tr>
<tr>
<td>Iron and steel production (CO₂ from 1.A.2.a +2.C.1)</td>
<td>– 105</td>
</tr>
<tr>
<td>Residential: fuels (CO₂ from 1.A4.b)</td>
<td>– 140</td>
</tr>
<tr>
<td>Manufacturing industries (excl. iron and steel) (energy-related CO₂ from 1.A.2 excl. 1.A.2.a)</td>
<td>– 299</td>
</tr>
<tr>
<td>Public electricity and heat production (CO₂ from 1.A.1.a)</td>
<td>– 346</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>– 1 382</strong></td>
</tr>
</tbody>
</table>


Primary steering effect:
Reduce GHG reduction from road transport sector, which is the only major sector with increasing emissions.

Annual revenue estimate\(^{115}\):

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Background:
The transport sector is the only major sector in the European Union in which GHG emissions have increased, currently accounting for a fifth of total EU emissions. E-mobility, the environmental consequences of which need to be discussed, is only slowly taking off. Fossil fuel-powered cars and lorries still largely dominate automotive sales across the EU. In addition, the price advantage of diesel due to preferential taxation across nearly all EU member states has led to a 50% market share for diesel when it comes to new car sales – unique among other industrialised regions in the world. Europe is not only falling behind on technology but also risks missing its emission reduction trajectory to 2050 if the current patterns of road transport remain unaltered.

Rationale
While emissions have dropped in almost every economic sector in the past 25 years, those stemming from road transport keep increasing, growing by 124 million tonnes of CO₂ equivalent since 1990. If the EU wants to advance on its climate and energy targets for 2030 and cut 40% of its GHG emissions from 1990 levels, it needs to find viable solutions to tackle these disconcerting emission trends in the transport sector.

Additionally road transport is a major contributor to other air pollutants detrimental for human health and the environment. In particular, road transport, especially diesel, contributes 30% of total EU emissions of nitrogen oxides (NOₓ), a pollutant whose concentration levels exceed EU air quality standards in urban areas across Europe. Air pollutants are the root cause of around 400,000 premature deaths in the EU-28 in 2012.

Added value as a Green Own Resource
Road fuel taxation is highly fragmented in the EU. Most countries apply different rates to petrol and diesel which in turn also feeds into distortive signals for consumers in terms of mobility choice. Petrol rates vary between EUR 0.77 per litre in the Netherlands and half this level – EUR 0.36 per litre – in Bulgaria, while diesel rate differences are even more pronounced, ranging between EUR 0.68 per litre in the UK and EUR 0.28 per litre in Portugal. These high gaps in road transport tax rates encourage fuel tourism, particularly favouring centrally located transit countries with relatively low tax rates such as Luxembourg. Due to the significant differences in diesel taxation between Luxembourg and its neighbouring countries, the sale of diesel per person is 5 to 8 times higher than in Germany, Belgium and the Netherlands and generates fuel tax revenues per inhabitant 4 to 5 times higher.

Countries taxing just above the minimum rate set out in the Energy Tax Directive while other countries apply taxes double the minimum rate create incentives for unnecessary fuel tourism especially in border regions and transit countries. There are 71 borders within the EU, and between EU member states and non-EU neighbour countries, which separate different fuel tax regimes and thus create potential for tax competition. If EU fuel taxes were fully harmonised, this number could be reduced to 33 outside borders. Better coordination or a move towards tax harmonisation could end these discrepancies and their distortional effects for the
European economy and the environment. A more coherent application of the polluter pays principle in the transport sector through better targeted taxation could provide public health and environmental benefits, and support investment flows towards sustainable mobility.

Better coordination of tax rates is possible. Adjusting the minimum rates towards a more climate-friendly petrol/diesel ratio can provide better incentives for consumers and lead to a more efficient allocation of resources. Revenue derived from the current road fuel taxation already exceeds the financial volume necessary to finance the entire EU budget. Thus, own resources either partly or entirely based on road fuel taxation can constitute a substantial share of a future EU budget.

3.4.2 SWOT-Analysis for Road Fuel Taxes

European Union can drastically boost its efforts to reduce the environmental impacts of the transport sector, the only sector which still experiences greenhouse gas emission increases. Choosing road fuel taxes as a source for EU own resources gives the needed impetus for a more coherent European-wider approach to tackle road transport externalities.

<table>
<thead>
<tr>
<th>STRENGTHS</th>
<th>WEAKNESSES</th>
</tr>
</thead>
<tbody>
<tr>
<td>▪ Reverse the worrisome trend of increasing emissions from the transport sector</td>
<td>▪ Redistributive effects can vary regionally depending on available public transport options</td>
</tr>
<tr>
<td>▪ End the preferential tax treatment of diesel</td>
<td></td>
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<tr>
<td>▪ Reduce fuel tourism in Europe</td>
<td></td>
</tr>
<tr>
<td>▪ Incentivise the use of electromobility and speed up the transformation towards a low-carbon car fleet</td>
<td></td>
</tr>
<tr>
<td>▪ Improve public health by reducing air and noise pollution from road transport</td>
<td></td>
</tr>
<tr>
<td>▪ High revenue potential: EUR 167 bn (2013) – could replace entire existing own resources</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>OPPORTUNITIES</th>
<th>THREATS</th>
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</thead>
<tbody>
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<td></td>
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</tbody>
</table>

EU progress so far

Excise duties on road transport fuels are governed by the Energy Tax Directive (Council Directive 2003/96/EC). The Directive foresees minimum rates on taxation of energy products, currently set at EUR 0.33 per litre for diesel and EUR 0.36 per litre for unleaded petrol. However, these rates are set too low to address the polluter pays principle and they leave too much divergence between road fuel taxation rates across the EU. In 2011, the European Commission proposed to revise the Energy Tax Directive by inter alia introducing tax parity to diesel and petrol, applying a minimum rate of EUR 0.38 per litre to each. The proposal was however frustrated by the Council and ultimately withdrawn by the Commission.

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122 In 2013 total tax revenues from transport fuel excises amounted to EUR 167.4 billion while the EU’s annual budget of the same year was EUR 139.7 billion. Potential own resource estimates from road fuel tax of the HLGOR account for 0.2% or 0.3% of GNI, equivalent to approximately EUR 30–40 billion for a partial transfer (HLGOR, 2016). Thöne (2016) suggests that a full transfer of road fuel tax revenue could yield more than EUR 160 billion, enough to finance the entire EU budget. Thöne (2016). Transferring Taxes to the Union: The Case of European Road Transport Fuel Taxes. In The Future of EU-Finances, Working Papers for the Brussels Symposium on 14 January 2016. FiFo Institute for Public Economics at the University of Cologne. Accessed on 01.10.2016.
3.4.3 Key messages for Road Fuel Taxes

Table 5: Key messages per target group supporting road fuel tax as a Green Own Resource

<table>
<thead>
<tr>
<th>Road Fuel Tax</th>
<th>ECONOMY</th>
<th>SUSTAINABILITY</th>
<th>SOCIAL</th>
<th>EUROPE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Green Community</td>
<td>Efficient transport market, Low-carbon mobility</td>
<td>Low-carbon transport transition, End tax advantage for diesel, Improve air quality</td>
<td>Social effects</td>
<td>Sustainable mobility</td>
</tr>
<tr>
<td>Citizens</td>
<td>Efficient transport market</td>
<td>Low-carbon transport transition, Improve air quality</td>
<td>Social effects</td>
<td>Sufficiency</td>
</tr>
<tr>
<td>Local Councillors</td>
<td>Low-carbon mobility</td>
<td>Low-carbon transport transition, Improve air quality</td>
<td></td>
<td>Sustainable mobility</td>
</tr>
<tr>
<td>Industry</td>
<td>Efficient transport market, Low-carbon mobility</td>
<td></td>
<td></td>
<td>Sustainable mobility</td>
</tr>
<tr>
<td>Member states</td>
<td>Efficient transport market, Low-carbon mobility</td>
<td>End tax advantage for diesel, Improve air quality</td>
<td>Social effects</td>
<td>Sufficiency, Sustainable mobility</td>
</tr>
</tbody>
</table>

ECONOMY

**Efficient transport market**: “Better alignment of road fuel tax rates is necessary to combat significant market inefficiencies.”

**Target Groups**: Green community, citizens, industry, member states

The existing differences in road fuel taxes across the EU, with some countries applying rates close to the minimum rates established in the EU Energy Tax Directive and others taxing considerably higher leads to a number of market distortions. Luxembourg is a main beneficiary to the detriment of its neighbours. Sales of diesel per person is 5 to 8 times higher, in the Grand Duchy than in Germany, Belgium and the Netherlands and generate fuel tax revenues per inhabitant 4 to 5 times higher. Better coordination of road fuel taxes could make revenue generation and distribution fairer, more efficient and less distortive.

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Low-carbon mobility: “Europe must not fall behind other regions in developing leading low-carbon mobility technology.”

Target Groups: Green community, local councillors, industry, member states

A quarter of total cars worldwide is still produced in Europe giving the car industry primary importance in EU international trade\textsuperscript{124}. Figure 9 shows that the EU is leading in the global export volume of motor cars. Yet, should the EU not wake up to future technological and innovation trends, it will fall behind other regions thereby jeopardising its export revenue as well as its role as a big player on the international car market. While other countries and regions have made impressive advances in the production and sales of electric and hybrid cars, European car manufacturers have manoeuvred the continent into the questionable international lead on diesel cars sold. Diesel accounted for 53% of new car sales in Western Europe in 2014, compared to 1–5% in Japan and the US, home to Nissan and Tesla which are currently market leaders in the electric car segment\textsuperscript{125}. This is partially the result of preferential tax rates for diesel alongside a focus on diesel car production by Europe’s long-established car industry. Europe needs to better orchestrate its road fuel tax policies and bring it in line with its long-term objectives of sustainable and affordable mobility.

SUSTAINABILITY

Low-carbon transport transition: “A European budget based on road fuel taxes can boost the EU-wide transition towards low-carbon mobility and reduce EU transport emissions.”

Target Groups: Green community, citizens, local councillors

Road transport emissions are a major and increasing contributor to the EU’s total emissions and still lack a comprehensive approach towards decarbonisation. With the vast majority of the EU’s car fleet and production currently locked into fossil fuel powered technology, this trend is likely to

Figure 8: EU and other major players in world-wide trade in motor cars in 2010


continue unless member states start to give structural signals which incentivise more climate-friendly means of mobility. A European-wide strategy to align existing road fuel taxes could gradually achieve a transformation of the EU mobility system towards low-emission modes of transport, the expansion and diversification of public transport networks, and the effective reduction of EU transport greenhouse gas emissions in the medium and long term.

**End tax advantage for diesel:** “A carbon-neutral minimum tax rate can help to eliminate the inefficient and climate-damaging preferential taxation of diesel.”

**Target Groups:** Green community, member states

Diesel enjoys a preferential tax treatment in all EU member states except the UK, the only country which applies a petrol-diesel parity tax rate. In every other country diesel is taxed less than gasoline. This distortion in favour of diesel works against the EU’s efforts to reduce greenhouse gas emissions from the transport sector, since diesel produces more CO\(_2\) per litre than gasoline\(^{126}\). EU own resources from road fuel taxes should therefore be based on EU-wide minimum rates which undo the distortive preferential tax treatment of diesel. The proposal to revise the Energy Tax Directive already foresaw a tax parity minimum level between diesel and petrol of EUR 0.38 per litre similar to the tax parity in the UK\(^{127}\).

In order to achieve a CO\(_2\)-neutral tax ratio however, the EU road fuel own resource could be

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\(^{126}\) According to Thöne (2016), diesel produces 2.64 kilograms of CO\(_2\) per litre compared with 2.33 kilograms per litre for gasoline, leading to a CO\(_2\) neutral tax ratio of gasoline/diesel of 0.88 (see figure 2). Thöne, M. (2016). Transferring Taxes to the Union: The Case of European Road Transport Fuel Taxes.


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**Figure 9:** Gasoline/diesel tax rate ratios in EU member states compared to CO\(_2\)-neutral ratio in 2015

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**Source:** Thöne, M. (2016). Transferring Taxes to the Union: The Case of European Road Transport Fuel Taxes.
based on minimum rates for diesel and petrol which place a higher burden on diesel relative to gasoline.\(^\text{128}\)

**Improve air quality:** “Better road fuel tax alignment can reduce air pollution and improve public health, especially in urban centres.”

**Target Groups:** Green community, citizens, local councillors, member states

Car emissions, particularly in urban agglomerations, are a significant source of air pollutants with detrimental effects on public health and air quality in cities. The concentration of nitrogen oxides (NO\(_X\)) is especially alarming as transport emissions have grown faster and real-world emissions, particularly from diesel cars, were found to be much dirtier than it had been expected and estimated.\(^\text{129}\) The scandal surrounding large-scale and systematic manipulations of diesel cars by the industry has undermined the trust in producers’ capacity to deliver the low-carbon technology needed for the mobility transition. By orchestrating road fuel taxes policymakers could provide consumers and producers a clear signal that fossil fuel powered mobility with all its accompanying harmful pollutants needs to give way to cleaner, more diverse and more sustainable modes of mobility.

**Socia**

**Social effects:** “Road fuel taxes are on average less regressive than other forms of taxation while providing for better air quality and more sustainable modes of transport.”

**Target Groups:** Green community, citizens, member states

Road fuel taxes have very heterogeneous consequences on income redistribution depending on the existing alternatives to road transport, wealth distribution among urban and rural population groups and the country’s overall economic situation. Yet, in comparison with other forms of taxation, road fuel tax is less regressive, especially in countries with a lower GDP per capita.\(^\text{130}\) Moreover, country-specific compensatory measures can help to alleviate undesired distributional effects. These measures should be communicated with a focus on public goods which well-orchestrated road fuel taxes can deliver in the medium term, ranging from better air quality to a shift in investment towards sustainable and low-carbon public transport schemes.

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**Europe**

**Sufficiency:** “A full transfer of road fuel taxes could generate enough resources to replace the entire EU budget.”

**Target Groups:** Citizens, member states

Total revenue from road fuel taxes account for more than EUR 160 billion per year in the EU.\(^\text{131}\) Compared to an annual EU budget of around EUR 145 billion, a total transfer of road fuel taxes from the member states – even if politically unlikely – could replace the entire EU budget. Should member states not agree to pass road fuel tax revenue completely on to the European level, a road fuel based own resource made up of a partial transfer could still constitute a substantial share of a future EU budget.

**Sustainable mobility:** “Decarbonising mobility is a prime objective for meeting the commitments of

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128 For example a petrol/diesel ratio of 0.88 (see footnote 122 – previous page).


130 According to Flues et al. (2015), on an expenditure basis transport fuel taxes can have on average “clear progressive distributional effects” in poorer OECD countries, while countries with higher GDP per capita experience more proportional and slightly regressive effects. Other studies (Ekins and Speck, 2011; Vivid Economics, 2012) suggest that in comparison to energy taxation or direct forms of taxation, fuel taxes have been less regressive, imposing relatively smaller burdens on the poor and a larger burden on those in the middle.

131 Figure for 2013, total tax revenue from transport fuel excises. Thöne, M. (2016). Transferring Taxes to the Union: The Case of European Road Transport Fuel Taxes.
the Paris Agreement and the 2030 Sustainable Development Agenda.”

**Target Groups:** Green community, local councillors, industry, member states

Road fuel tax coordination can deliver a crucial contribution to the Paris Agreement target. In October 2016 the EU agreed to drastically reduce its greenhouse gas emissions with the goal of limiting climate change well below 2°C. According to the European Commission’s analysis, the transport sector, being the only sector that has experienced a significant increase in emissions since 1990, needs to achieve a reduction in greenhouse gas emissions of at least 60% as compared to 1990 levels by 2050\(^{132}\). Disincentivising the use of fossil fuel-powered vehicles can shift investments towards low-carbon transport alternatives, including public transport and electromobility. This is also in line with the 2030 Sustainable Development Agenda which foresees providing access to “safe, affordable, accessible and sustainable transport systems for all, notably by expanding public transport”\(^{133}\).

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3.5 EU Air Ticket Tax

3.5.1 EU Air Ticket Tax Profile

Definition:
Green Own Resource based on an EU carbon-based air ticket tax.

Key figure:
Projected CO2 emissions from international aviation.

Source: IEA 2014, ICAO 2013b, Lee et al. 2013


Primary steering effect:
GHG emission reduction from aviation.

Annual revenue estimate\(^{134}\):

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Background:

Air traffic is the most climate-intensive form of transport and also the fastest growing transport mode. By 2030 CO₂ emissions from aviation are expected to rise by 300%\(^{135}\). Domestic and international aviation account for 6% of total GHG emissions in the EU, representing 13% of emissions from the transport sector\(^{136}\). However, aviation enjoys a very favourable tax treatment enshrined in European and international law. Neither fuel tax, nor VAT are currently levied on air transport and even under the ETS only 25% of GHG emissions caused by aviation are captured, since only flights within the EU airspace are accounted for\(^{137}\). In 2016, the total potential tax revenue lost through these tax exemptions which are equivalent to an indirect subsidy was estimated to amount to EUR 40 billion and is likely to double by 2030\(^{138}\).

Rationale:

The tax exemption of the aviation sector is a giant market distortion. No other mode of transport enjoys as profound preferential tax exemptions. The difficulties in bringing about change, notably via the International Civil Aviation Organisation (ICAO), have created a context in which taxes on aviation are not subject to a race-to-the-bottom as in the context of corporate tax or road fuel tax, but are rather “stuck at the bottom”\(^{139}\). At the same time, aviation is by far the most carbon-intensive form of transport, with substantial growth potential in the coming decades. A prominent model of an EU air ticket tax based on flight-specific carbon intensity has been suggested by Margit Schratzenstaller and Alexander Krenek in the context of the FairTax project in May 2016\(^{140}\). Although their model assumes a relatively low carbon price of EUR 35 per tonne of CO₂ as their high tax scenario, their proposal is a noteworthy basis for a Green Own Resource candidate.

Added value as a Green Own Resource

Introducing an EU Green Own Resource based on an air ticket tax could alleviate the blatant inconsistencies between the EU’s climate objectives and the preferential tax treatment of the aviation sector as well as restoring overall fairness and just competition in the transport market. The tax revenues foregone through VAT and fuel tax exemption to the aviation industry, amounting to approximately EUR 40 billion annually, distort competition and constitute indirect environmentally harmful subsidies which are contradictory to the EU’s greenhouse gas emission reduction targets. Due to the legal obstacles in taxing kerosene, charges on flight tickets, preferably taking into account distance or carbon intensity, is a way to internalise the environmental costs of aviation without infringing international tax restrictions.

EU progress so far

In the past, several European countries have unilaterally introduced, or at least attempted to, a levy on flights or flight tickets, partially to


internalise the detrimental climate effects of aviation. Regrettably, the number of European countries which have eventually scrapped their flight ticket tax is almost as large as the group of countries which still apply the levy domestically\(^1\)\(^4\). This is evidence of the inadequacy of unilateral member state approaches to tax aviation.

GHG emissions from the aviation sector are included in the EU Emission Trading Scheme (EUETS). In the beginning of 2012 flights within the EU as well as intercontinental flights were included in the ETS while 85% of all emission allowances were allocated for free. Later, from 2013 to 2016, flights outside the European Economic Area were exempted from ETS requirements to allow the ICAO to develop a global mechanism. Free certificate allocation, or “Grandfathering”, is expected to continue in future\(^1\)\(^4\). At the same time, the aviation sector is globally undertaxed. On an international level, the Chicago Convention of 1944 which established the International Civil Aviation Organisation (ICAO) provides for the worldwide exemption of international flights from mineral oil tax. Current negotiations on global measures to tackle GHG emissions from aviation have recently led to the adoption of a Global Market-Based Mechanism called CORSIA (Carbon Offsetting and Reduction Scheme for International Aviation), but doubts remain on whether this voluntary scheme will prove effective in achieving carbon-neutral growth for aviation in time\(^1\)\(^4\). On a European level, article 148 of the EU VAT Directive (2006/112/EC) exempts air transport of fare-paying passengers from VAT while article 14 EU Energy Tax Directive (2003/96/EC) obliges member states to create kerosene tax exemptions for international flights.

### 3.5.2 SWOT-Analysis for EU Air Ticket Tax

Taxing air tickets can help to internalise the social costs of aviation and create incentives both for individuals to refer to other, less carbon-intensive modes of transport, and for industry to increase investments in low-emission aviation technology.

The free rider problem poses a potential threat as evidenced by the high number of countries which have abolished the air ticket tax after a unilateral introduction.

<table>
<thead>
<tr>
<th>STRENGTHS</th>
<th>WEAKNESSES</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Internalise part of the environmental costs of aviation</td>
<td>- Second best option as the carbon carrier, namely the fuel, cannot be taxed directly</td>
</tr>
<tr>
<td>- Circumvent the VAT and kerosene tax exemptions currently in place to restore fairness in the transport sector</td>
<td>- Inclusion of intercontinental flights challenging</td>
</tr>
<tr>
<td>- EU-wide approach most efficient system before global mechanism</td>
<td></td>
</tr>
<tr>
<td>- Restore fair competition in the transport sector</td>
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Table 6: Key messages per target group supporting an EU air ticket tax as a Green Own Resource

3.5.3 Key messages for EU Air Ticket Tax

**ECONOMY**

Fair transport competition: “An EU air ticket tax can effectively circumvent the unjustifiable tax exemptions of aviation and restore fairness in the transport market.”

Target Groups: Green community, citizens, local councillors, industry, member states

Aviation enjoys unique VAT and fuel tax exemptions which put the sector at an unjustifiable advantage in comparison with other, often less carbon-intensive, modes of transport. International provisions stemming from the 1944 Chicago Convention have ensured that the tax exemptions which were meant to promote the growth of a then young transport industry, have continued to be effective until today. Should
aviation be treated similarly to other transport sectors in terms of tax contributions, estimates suggest potential tax returns of EUR 7.1 billion from VAT and EUR 20 to 32 billion from fuel taxes per year. The total estimate of approximately EUR 40 billion constitutes an indirect subsidy. The original intention of the tax exemptions to boost growth of the aviation sector in mid-twentieth century have overshot its target. Between 1990 and 2014, the number of flights has increased by 80% and forecasts suggest another 45% growth until 2035. It is time to realise that the tax advantage of aviation is counter to the EU’s objectives on achieving a competitive and resource-efficient transport system as stipulated in the European Commission’s 2011 White Paper on Transport and needs to be corrected. An EU carbon-based air ticket tax as suggested by Schratzenstaller and Krenek could contribute to this process.

**Push low-carbon aviation:** “Internalising the carbon-intensity of flying can create investment incentives boosting research in low-carbon aviation technology and alternative fuel.”

**Target Groups: Industry, member states**

An EU air ticket tax would add a charge to each individual ticket based on the carbon intensity of the respective flight. This provides market signals indicating the most carbon-efficient competitor among airlines and aircraft manufacturers. Price incentives such as those created through a carbon-based ticket tax could build up pressure to crank up investments into sustainable aviation fuel and more carbon-efficient aircraft technology.

**SUSTAINABILITY**

**Improve aviation’s environmental footprint:** “An EU air ticket tax can curb GHG emissions from aviation, increase the share of more sustainable fuel in the transport sector and reduce other harmful externalities such as air pollution and noise.”

**Target Groups:** Green community, citizens, local councillors, industry, member states

Aviation needs better market signals to incentivise more sustainable development. Alongside the increase in passenger numbers, CO₂ emissions have also grown by about 80% between 1990 and 2014. NOₓ emissions have doubled at the same time and are estimated to increase further. Between 2014 and 2035, CO₂ emissions are expected to grow by 45%, NOₓ emissions by 43%. Reduced flight numbers as a consequence of an EU air ticket tax could dampen these growth rates and increase incentives to shift investment towards abatement technology of NOₓ and CO₂. This would also help to mitigate other negative externalities. For example, currently, around 2.5

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149 Estimates by Schratzenstaller & Krenek show that an air ticket tax based on a carbon price of EUR 35 could dampen the growth rates in air passengers in most of the EU member states and reduce or stagnate rates in around a third of member states, including Germany, Austria and Sweden). Relevant data is already available using the ICAO methodology. Schratzenstaller & Krenek (2016). Sustainability-oriented EU Taxes: The Example of a European Carbon-based Flight Ticket Tax. FairTax [Working Paper](https://doi.org/10.1007/978-3-642-33077-9_6) Series No.01. Accessed on 01.10.2016.
62 million people are exposed to noise at 45 major European airports.

**Incentivise use of sustainable fuel:** “Investments into alternatives to carbon-intensive kerosene can enhance the use of and research into alternative biofuels.”

**Target Groups:** Green community, industry, member states

According to the 2011 White Paper on Transport, the European aviation industry should “become a front-runner in the use of low-carbon fuels” by reaching a share of low-carbon sustainable fuels in aviation of 40% by 2050. The European Aviation Environmental Report (2016) underlines that although potential emissions savings from alternative sustainable fuels may be as large as 80%, biofuels are only slowly entering the market. Should the EU choose a tax that accounts for actual carbon intensity per flight, market pressure on the deployment of more sustainable aircraft fuels would support the EU’s efforts in achieving low-carbon aviation.

**SUSTAINABLE**

**Progressive tax on flying:** “Frequent fliers would be the main contributors to the tax.”

**Target Groups:** Green community, citizens, local councillors, member states

Flying is a luxury. In economic terms this is indicated by a good’s Engel-elasticity which is relatively high for air travel. That means that the willingness to spend money on air tickets varies largely with changes in disposable income. Taxing luxury goods with higher elasticities generally yields progressive distribution effects. Frequent users of aviation as a mode of transport would be the main contributors to such a levy which underlines the progressive potential of the air ticket tax. This potential progressivity can be further pronounced by charging a higher tax on business class than on economy class which is the case in France. This is why in their 2015 study on global inequality, Piketty and Chancel propose a progressive flight ticket tax targeting higher-income earners in order to finance the Green Climate Fund. Their proposal comprised taxes on business class tickets at a rate of EUR 180 and EUR 20 on economy class tickets. While the specific rates applied can still be subject to debate, the inclusion of class categories can prove an effective complement to support the air ticket tax’s progressive effect on income distribution.

**EUROPE**

**Sustainable transport agenda:** “Aviation needs to be addressed in the context of the Sustainable Development Agenda.”

**Target Groups:** Green community, local councillors, industry, member states

The Sustainable Development Goals set out a clear vision of sustainable transport under Goal 11.2. Currently, a High Level Advisory Group on Sustainable Transport (HLAG-ST) is working on recommendations for policymakers around the world to improve sustainability of different modes of transports including aviation. The policy recommendations developed by the HLAG-ST are expected to be reflected in a global sustainable transport outlook report that will be released in a

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first international conference on sustainable transport in November 2016.

**Collective action necessary:** “EU-wide approach alleviates the free rider problem and the relocation of airlines.”

**Target Groups:** Green community, citizens, local councillors, member states

A main concern of regional level policymakers and member states is the potential relocation of airport passengers to neighbouring airports if a surcharge is introduced unilaterally. This was, for example, the case in the Netherlands, which suspended its *Vliegbelasting*, Air Passenger Duty, only one year after it was introduced. The Dutch case shows that particularly small countries are vulnerable to experiencing passenger decrease in response to their domestic action, rendering the tax economically harmful and environmentally ineffective. An EU-wide introduction could remedy these concerns and underline the suitability and need to boost efforts on the European level.

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3.6 EU Financial Transaction Tax

3.6.1 EU Financial Transaction Tax Profile

Definition:
Green Own Resource based on a tax applied to financial transactions of securities (0.1%) and derivatives (0.01%).

Key figure:
Infographic on FTT, EU budget (2012) and total bailout costs during the financial crisis.


Primary steering effect:
Financial market stability and sustainability.

Annual revenue estimate:\(^{156}\):

Background:
The financial crisis of 2008 triggered a number of unprecedented political interventions to keep financial institutions all over the EU from collapsing. According to the European Commission, state aid measures amounting to EUR 4.5 trillion – representing 37% of EU GDP – were granted by EU governments to bolster systemic risk in the financial sector between October 2008 and October 2011\(^\text{157}\). Socialising the financial cost of the crisis revealed systemic deficits in the public finances of a number of member states and has plunged the entire EU economy into peril leading the EU GDP to contract by 4.2% or EUR 0.7 trillion in 2009\(^\text{158}\).

Rationale:
On an aggregate level, European taxpayers, not the institutions involved in years of dubious financial operations paid the lion’s share and keep doing so as Europe has been thrown into the deepest recession since the Second World War. Although supervision of financial institutions increased – i.e. through the establishment of supervisory bodies such as EBA, ESMA, EIOPA as well as advances towards a European Banking Union – incentives for individual behaviour are still unaltered and allow harmful high-risk transactions.

Added Value as a Green Own Resource
Despite the general consensus that insufficient regulation of the financial sector and its key institutions in Europe and the US lay at the core of the outbreak of the crisis, regulatory measures addressing these vulnerabilities have been slow and rather patchy. Legislative action in reaction to the crisis has mainly focused on financial supervision and better risk assessment. The incentive structure permitting and amplifying detrimental financial activities has survived the crisis largely unaltered. A European financial transaction tax (FTT) could, either applied to all member states or to a group of willing countries under enhanced cooperation, create better incentive structures which may contribute to stabilising the financial sector and making it less vulnerable to future crises. At the same time key financial institutions would come to share part of the burden of the financial crisis and contribute to long-term market sustainability by reducing the systemic risk of overall transactions.

EU Progress so far
Several European member states have already introduced some forms of national FTT in the past\(^\text{159}\). However, rates and tax bases vary widely with some countries applying capital and stamp duties and other taxes on transactions. However, especially in the 1990s, there has been a general trend towards the abolishment of national FTTs.

The introduction of an EU FTT has been a long and winding road and is yet to be completed. In 2011, the European Commission presented its proposal for a FTT, also discussing its potential as a source for future EU own resources. The proposed FTT had three principle objectives: first, enhance market stability and proper functioning of the financial market. Second, ensure that the financial sector pays a “fair and substantial” contribution to the overall costs of the economic crisis\(^\text{160}\). Third, discourage transactions which are harmful to financial market stability and efficiency. Subsequently, negotiations stagnated due to inter alia strong opposition by the UK. In 2013, the Commission proposed the introduction of a FTT


\(^{159}\) These countries are Belgium, Denmark, Finland, Germany, Ireland, the Netherlands, Poland, Spain, Sweden and the UK.

under the so-called “enhanced cooperation” for originally 11, now 10, willing member states\(^{161}\), but negotiations in the Council have proved cumbersome leaving the formal adoption of the tax to be postponed several times\(^{162}\). The current proposal foresees that the tax applies to all financial transactions with rates of 0.1% of the price for transactions on securities and 0.01% for derivative products. The tax would apply as soon as at least one of the parties to the transaction is established in a member state participating in the enhanced cooperation. However, discussions are still ongoing. Furthermore, in the medium term, the 2016 Brexit could become a game changer in the debate of a broad-based FTT as a strong candidate for a future Green Own Resource for the EU.

### 3.6.2 SWOT-Analysis for Financial Transaction Tax

An EU financial transaction tax has the potential of providing more economic sustainability by addressing some of the main deficiencies in the financial sector. Most uncertainties about the EU FTT as an own resource currently stem from the implications on variable geometry or whether a potential own resource should be based on an instrument applied only in a fraction of member states and whether a later expansion to all member states could be envisaged as part of a gradual introduction of an FTT to the entire EU.

<table>
<thead>
<tr>
<th>STRENGTHS</th>
<th>WEAKNESSES</th>
</tr>
</thead>
<tbody>
<tr>
<td>▪ Enhance the proper functioning of the internal market for transactions in financial instruments</td>
<td>▪ Relatively low initial taxation rates</td>
</tr>
<tr>
<td>▪ Ensure that financial institutions pay a fair and substantial contribution to the costs of the financial and economic crisis</td>
<td>▪ Variable geometry with proceeds from only 10 member states could add to the complexity of the budget</td>
</tr>
<tr>
<td>▪ Create disincentives for transactions which are harmful to overall efficiency and stability of financial markets</td>
<td>▪ Scope of FTT jurisdiction uncertain due to Brexit</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>OPPORTUNITIES</th>
<th>THREATS</th>
</tr>
</thead>
<tbody>
<tr>
<td>▪ Large public support in favour of making the financial sector contributing its fair share</td>
<td>▪ Slow progress and backlash under enhanced cooperation procedure</td>
</tr>
<tr>
<td>▪ Supports Sustainable Development Goal 10.5 on financial market regulation</td>
<td>▪ Current struggle of systemically important banks (Deutsche Bank, Banca Monte dei Paschi)</td>
</tr>
<tr>
<td>▪ Brexit could reopen negotiations for an EU-wide FTT</td>
<td>▪ FTT could provide more stability in the long run</td>
</tr>
</tbody>
</table>

\(^{161}\) These countries are Belgium, Germany, Greece, Spain, France, Italy, Austria, Portugal, Slovenia, and the Slovak Republic. Estonia was originally part of the cooperation but later disembarked from the negotiations.

3.6.3 Key messages for Financial Transaction Tax

Table 7: Key messages per target group supporting an EU FTT as a Green Own Resource

<table>
<thead>
<tr>
<th>EU FTT</th>
<th>ECONOMY</th>
<th>SUSTAINABILITY</th>
<th>SOCIAL</th>
<th>EUROPE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Green Community</td>
<td>Financial market stability</td>
<td>Sustainable finance for sustainable markets</td>
<td>Fair and substantial</td>
<td>Borderless market</td>
</tr>
<tr>
<td></td>
<td>Circumvent VAT exemption</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Citizens</td>
<td>Financial market stability</td>
<td>Sustainable finance for sustainable markets</td>
<td>Fair and substantial</td>
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</tr>
<tr>
<td></td>
<td>Circumvent VAT exemption</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Local Councillors</td>
<td>Financial market stability</td>
<td>Sustainable finance for sustainable markets</td>
<td>Fair and substantial</td>
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<td></td>
<td>Circumvent VAT exemption</td>
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<tr>
<td>Industry</td>
<td>Financial market stability</td>
<td>Sustainable finance for sustainable markets</td>
<td>Fair and substantial</td>
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<td></td>
<td>Circumvent VAT exemption</td>
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<tr>
<td>Member states</td>
<td>Financial market stability</td>
<td>Sustainable finance for sustainable markets</td>
<td>Fair and substantial</td>
<td>Borderless market</td>
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<tr>
<td></td>
<td>Circumvent VAT exemption</td>
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</table>

**ECONOMY**

**Financial market stability:** “Discouraging high-risk transactions can help to prevent future financial crises.”

**Target Groups:** Green community, citizens, industry, local councillors, member states

A prime objective of the FTT proposed by the European Commission is to stabilise the volatile financial market by reducing undesired market behaviour. The FTT targets in particular transactions with excessively high-risk investments thereby internalising the systemic risk they pose to the financial sector at large. The Commission also expects that taxes on high-frequency trading could create incentives for financial institutions to shift their investment strategies to sustained investments rather than pure short-term profit-seeking trading.

**Circumvent VAT exemption:** “Taxing financial transactions can at least partially remedy the generous VAT exemption of most financial services in the EU.”

**Target Groups:** Green community, citizens, local councillors

In general, most mainstream financial service providers including insurances and investment banking have been exempt from the EU’s common value added tax system. Article 135(1) of the EU VAT Directive (2006/112/EC) provides an exemption from VAT for most financial and insurance services. The exemption means that VAT is not charged to clients of financial services. This fiscal advantage has an estimated magnitude of

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0.11 to 0.17% of GDP\textsuperscript{164}. Since such VAT exemptions are applied in many countries across the world, experts have stressed that the global financial sector is generally undertaxed\textsuperscript{165}.

**SUSTAINABILITY**

**Sustainable finance for sustainable markets:** “The FTT can help to align financial activities with real economy activities.”

**Target Groups:** Green community, citizens, local councillors, industry, member states

As a financial transaction tax discourages transactions with a high risk association, one of their prime objectives is to limit potentially harmful high-frequency trading and to contribute to financial activity which is more in line with the activity level of the real economy. The decoupling of financial operations from real economy activities which became evident with the substantial expansion in financial transaction volume in the early 2000s has prepared the ground for the formation of the financial bubbles which lay at the heart of the 2008 crisis. According to the German Economic Research Institute (DIW), an effective FTT could reduce the number of transactions, particularly in derivative trading and contribute to more sustainability of financial markets\textsuperscript{166}.

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**SOCIAL**

**Fair and substantial:** “Taxing the financial sector can rebuild trust and bring about progressive burden sharing of the costs of the crisis.”

**Target Groups:** Green community, citizens, local councillors, member states

Although the exact costs of the financial crisis in Europe are difficult to quantify, the Commission estimates that they exceed 15 to 20% of EU27 GDP\textsuperscript{167}. Taking into account the medium-term consequences of the contraction of the EU economy due to the crisis, it is estimated that EU taxpayers financed at least EUR 4.5 trillion in state intervention. This is equivalent to 37% of EU GDP or more than 30 times the entire annual EU budget\textsuperscript{169}. This has led to a wide support of taxing the financial sector among citizens. Around 61% of Europeans support the principle of a financial transaction tax\textsuperscript{169}. Already in its 2010 Communication on Taxation of the Financial Sector, the European Commission underlined its intention to ensure that financial institutions pay a fair and substantial contribution to the burden of the crisis\textsuperscript{170}. Such a fair and substantial contribution is expected to amount to annual revenues in the order of 0.3% to 0.5% of EU GDP\textsuperscript{171}. Besides the argument of burden sharing, an FTT also has potential positive equity effects on economic actors by partially compensating for the
possible tax advantage of the financial sector due to the VAT exemption. In addition, financial assets are disproportionately owned by members of the upper income quintiles giving the tax an unambiguously progressive distributional impact\(^\text{172}\).

**EUROPE**

**Borderless market:** “The transboundary nature of the financial market makes proceeds from the FTT a likely candidate for EU own resources.”

**Target Groups:** *Green community, member states*

Regulating the proper functioning of the EU financial market is a transnational objective best fulfilled on a European if not on a global level. Since there doesn’t seem to be any meaningful effort for a global tax on financial transactions at the moment, an EU approach is the best option in reach. Due to the high mobility tax base, action at the EU level is preferable to national unilateral approaches. The high integration of the financial sector within the EU is another argument why the subsidiarity principle upholds in the case of an EU FTT. Likewise, the difficulty to clearly determine attributability of proceeds underlines the suitability of the FTT to finance the EU budget. Revenue estimates of an EU FTT vary according to the scope and design options of the tax\(^\text{173}\).

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\(^{173}\) In a forthcoming publication of the FairTax Project, expected to be published in November 2016, Solilová, Nerudová, and Dobranschi provide a detailed overview of estimates of different FTT design options under various elasticity assumptions. Their results indicate that a common FTT levied on the countries participating in the enhanced cooperation or the entire EU could pool enough aggregate revenue to fully replace current VAT- and GNI-based contributions. Solilová et al. (2016). Sustainability-oriented Future EU Funding: The case for FTT. Paper presented during the FAIRTAX Conference “Options for an EU Tax as an EU Own Resource” in Vienna on 19 September 2016. Publication forthcoming under the FairTax Project.
3.7 EU Corporate Income Tax

3.7.1 EU Corporate Income Tax Profile

Definition:
A European Corporate Income Tax (EU CIT) determining minimum corporate tax levels and based on a harmonised EU-wide tax base.

Key figure:
Comparison between volume of 2016 EU budget and estimated annual losses of tax avoidance in billion EUR.

Source: European Parliament (2015c). Bringing transparency, coordination and convergence to corporate tax policies in the European Union. EPRS.

Primary steering effect:
Fight against aggressive tax planning and protecting the proper functioning of the Internal Market.

Annual revenue estimate:\(^{174}\):
- EUR 15 billion
- In % of total EU budget: 10%
- In % of national contributions: 12%

Background:
EU-wide momentum on tackling tax avoidance has been reinvigorated mostly due to increased public awareness about tax justice after the economic crisis and several important leaks on large-scale tax avoidance, notably by large multinational enterprise (MNEs). Tax fraud and tax avoidance in Europe have reached an enormous scale, amounting to approximately EUR 1 trillion lost annually\(^{175}\). According to the European Parliament, EUR 160–190 billion, more than the entire annual budget of the EU, is lost every year in the EU due to corporate tax avoidance, aggressive tax planning and special tax arrangements\(^{176}\). Losses due to profit shifting alone is estimated to range between EUR 50–70 billion, equivalent to 17–23% of corporate income tax revenue in 2013\(^{177}\).

Rationale:
Such tax avoidance practices are made possible by a lack of tax coordination, giving member states the incentive to adopt strategically low corporate tax rates and grant special tax arrangements and deals to multinational enterprises. Recent developments show a downward trend across EU member states in the share of corporate income tax revenue of total tax revenue\(^{178}\). This race to the bottom prevents any comprehensive approach to address the social consequences of tax avoidance on such a colossal scale. Besides the losses for tax authorities and society at large, aggressive tax planning undermines the principle of fair, efficient and growth-friendly corporate taxation in which profits are taxed where they are generated. Undermining this principle distorts market prices and gives multinational companies an unfair advantage, particularly over small and medium-sized enterprises (SMEs)\(^{179}\).

Added Value as a Green Own Resource
Currently, member states not only apply different rates, but also apply their national corporate taxes to different tax bases, increasing the likelihood of fraud and impeding transparency and simplicity especially for transnational enterprises. A first step towards an EU common corporate tax is a harmonised tax base as it is currently prepared at the EU level. Besides paving the way for a comprehensive solution against the rampant avoidance of corporate taxes, the Common Consolidated Corporate Tax base (CCCTB) could bring more transparency to EU businesses with the potential to reduce tax-related company expenditure on average by 62% to 67%\(^{180}\). A subsequent EU corporate income tax in the form of a common minimum rate could generate own resources feeding into a future EU budget. Such a design would reduce tax competition among EU member states, create more coherence and fairness in the Internal Market, and could generate a substantial amount of revenue. In 2011 the European Commission estimated that an EU corporate income tax of less than 2% could

\(^{175}\) This figure includes potential tax revenue lost due to illegal (tax fraud and tax evasion) as well as legal (tax avoidance and aggressive tax planning) corporate practices. Broken down to the level of individual EU taxpayers, this figure represents costs of roughly EUR 2000 per citizen. On average, the amount of tax lost exceeds public expenditure on healthcare and is four times as high as member states’ spending on education. European Parliament (2013b). Report on Fight against Tax Fraud, Tax Evasion and Tax Havens, A7-0162/2013. Accessed on 01.10.2016.


\(^{178}\) Núñez Ferrer et al. (2016). Study on the potential and limitations of reforming the financing of the EU budget. Study commissioned by the European Commission on behalf of the High Level Group on Own Resources.

\(^{179}\) According to a study by Finke (2013), German multinationals paid 27 percent less taxes than purely domestically invested firms. Finke, K. (2013), Tax Avoidance of German Multinationals and Implications for Tax Revenue Evidence from a Propensity Score Matching Approach, mimeo.

generate annual revenues amounting to EUR 15 billion.\(^{181}\)

**EU Progress so far**

In considering modifications to the own resource system in the past, a potential EU corporate income tax has been a reoccurring candidate in the European Commission’s analyses.\(^ {182}\) Yet, there has been little progress on legislative action since 2011 when the European Commission proposed to establish a European Common Consolidated Corporate Tax base (CCCTB). After negotiations proved slow in the following years, European efforts were re-launched in 2015. The CCCTB is now discussed as part of a larger legislative package on Anti Tax Avoidance Package for a fairer, simpler and more effective corporate taxation. In late October 2016, the EU commission presented its proposal for two separate Directives on a CCTB and a CCCTB respectively.\(^ {183}\) EU-wide momentum on tackling tax avoidance has recently increased and is likely to remain high as a consequence of the LuxLeaks and Panama Paper revelations.\(^ {184}\)

### 3.7.2 SWOT-Analysis for EU Corporate Income Tax

EU member state income from corporate taxation has decreased in recent years, partially due to surges in tax competition. Common rules on CIT bases and rates throughout the EU could mitigate this competition and eliminate the highly distorting tax agreements to large corporations. The large variation of income tax regimes are a challenge to the adoption of an EU CIT, but recent leaks about aggressive tax planning by multinational corporations have revived a new momentum for progress on corporate taxation and the fight against tax avoidance.

<table>
<thead>
<tr>
<th>STRENGTHS</th>
<th>WEAKNESSES</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Establishes fairer effective taxation by eliminating loopholes and special tax arrangements for multinationals</td>
<td>• Current tax bases and tax rates are highly diverse in EU member states</td>
</tr>
<tr>
<td>• Improves the business environment for small and medium-size enterprises</td>
<td>• EU CIT necessitates smooth progress on CCCTB and subsequent consensus on CIT</td>
</tr>
<tr>
<td>• Eliminates the unfair market advantage of large multinational enterprises</td>
<td>•</td>
</tr>
<tr>
<td>• Ends the race to the bottom for corporate taxation due to tax competition</td>
<td></td>
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</tbody>
</table>


\(^{183}\) The Commission has suggested a step-wise establishment of a CCCTB, based on an agreement on a common corporate tax base (CCTB proposal) and a later consolidation (CCCTB proposal).

Key messages for EU Corporate Income Tax

3.7.3 Key messages for EU Corporate Income Tax

Table 8: Key messages per target group supporting EU CIT as a Green Own Resource

<table>
<thead>
<tr>
<th>EU CIT</th>
<th>ECONOMY</th>
<th>SUSTAINABILITY</th>
<th>SOCIAL</th>
<th>EUROPE</th>
</tr>
</thead>
</table>
| **Green Community** | ☐ Reduce tax competition
☐ Empower SMEs | ☐ Sustaining corporate tax income | ☐ Towards tax justice | ☐ United against tax avoidance |
| **Citizens**    | ☐ Reduce tax competition
☐ Empower SMEs | ☐ Sustaining corporate tax income | ☐ Towards tax justice | ☐ United against tax avoidance |
| **Local Councillors** | ☐ Reduce tax competition
☐ Empower SMEs | ☐ Sustaining corporate tax income | | ☐ United against tax avoidance |
| **Industry**   | ☐ Empower SMEs           | ☐ Sustaining corporate tax income | | |
| **Member states** | ☐ Reduce tax competition
☐ Empower SMEs | ☐ Sustaining corporate tax income | ☐ Towards tax justice | ☐ United against tax avoidance |

**ECONOMY**

Reduce tax competition: “A common EU regime on corporate taxation can end member states’ race to the bottom”

**Target Groups:** Green community, citizens, local councillors, member states

Corporate taxation within the EU is characterised by intense competition among member states to reduce their statutory and effective corporate tax rates. Between 2000 and 2012 a convergence to the bottom in CIT revenues as a percentage of GDP can be observed.

This observation is consistent with the decrease in the average statutory corporate tax rates in the EU, falling by 2.1% between 2005 and 2013. In comparison with other OECD countries, the deterioration of corporate tax rates is more pronounced in European countries, underlining the need for a common EU regime on corporate taxation.

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dynamics of distortive tax competition\textsuperscript{186}. The UK, which had already lowered its CIT by 10\% since 2008, has announced a further reduction of corporate taxes to a statutory rate of 17\% in 2020. It is time to establish common standards on corporate taxation throughout the EU to terminate this downward trend.

**Empower SMEs:** “Common rules on corporate taxation can facilitate procedures for SMEs and restore fairness in the Single Market”

**Target Groups:** Green community, citizens, local councillors, industry, member states

Multinational corporations, in contrast to small and medium-sized enterprises, possess the organisational and financial means to better exploit the lack of corporate tax coordination throughout the EU. According to a study by Finke (2013), German multinationals paid 27 percent less taxes than purely domestically invested firms\textsuperscript{187}. This also explains the estimated magnitude of tax losses due to aggressive tax planning and profit shifting. Moving to CCCTB and ultimately to a common EU CIT would significantly reduce the potential for aggressive tax optimisation and would constitute a logical consequence of the recent Commission efforts to enforce country-by-country reporting of profits for multinational firms.

**Figure 10:** Revenue from corporate income tax as a percentage of GDP in Eurozone countries

\textsuperscript{186} Jorge Núñez Ferrer et al. (2016). Study on the potential and limitations of reforming the financing of the EU budget. Study commissioned by the European Commission on behalf of the High Level Group on Own Resources. Accessed on 01.10.2016.

\textsuperscript{187} Finke, K. (2013), Tax Avoidance of German Multinationals and Implications for Tax Revenue Evidence from a Propensity Score Matching Approach, mimeo.
**SUSTAINABILITY**

**Sustaining corporate tax income:** “Aggressive tax avoidance is unjust, unsocial and unsustainable”

**Target Groups:** Green community, citizens, local councillors, industry, member states

There is general agreement that large-scale tax avoidance and aggressive profit shifting is harmful to national governments, individuals and businesses overall. In the context of the BEPS initiative (base erosion and profit shifting), the OECD estimated that profit shifting by multinational enterprises can lead to under-funding of public investment which could help promote overall economic growth. According to Friends of the Earth International (2016), foregone tax revenue due to tax evasion in the last 15 years could provide the investments necessary to achieve 100% renewable energy for half of the global population by 2030.

**SOCIAL**

**Towards tax justice:** “A common approach to corporate taxation throughout the EU can restore tax fairness and better aggregate income distribution”

**Target Groups:** Green community, citizens, member states

In its initiative report on base erosion and profit shifting (BEPS), the OECD has stressed that aggressive tax planning hurts individual taxpayers, since companies which are allowed to shift their income to different low-tax jurisdictions, the tax burden in the jurisdiction where the income is generated is shifted to local taxpayers, who have to shoulder a greater overall tax load. If no political action is taken, this trend will have repercussions on income equality in the Union. The EU should not miss this opportune moment to proceed on better tax coordination. A Eurobarometer in 2015 indicates that 87% of Europeans are in favour of tighter rules to tackle tax havens and tax avoidance, and this percentage is expected to increase or remain high after the LuxLeaks and Panama Paper revelations.

**EUROPE**

**United against tax avoidance:** “The highly distortive tax competition in the field of corporate taxation necessitates coordinated action”

**Target Groups:** Green community, citizens, local councillors, member states

The high variation among 28 different national corporate tax regimes impedes fair competition in the Internal Market. The Impact Assessment of the European Commission on the CCCTB has underlined the inefficiency of national unilateral action as it would have no effect on the overall variation of the European corporate tax landscape. Following the logic of the EU’s current advances under the Anti Tax Avoidance Package, a reconsideration of corporate minimum tax rates at the EU level deserves special attention, in particular with regards towards the better coordination of corporate tax information and regimes on a global level.

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3.8 EU Court of Justice Fines

3.8.1 CJEU Fines Profile

**Definition:**
Including proceeds from fines generated by rulings of the Court of Justice of the European Union (CJEU) as additional own resource revenue.

**Key figure:**
Fines imposed on companies for breaching EU competition law on cartels (TFEU Art. 101), 1990–2014.

![Graph showing fines imposed on companies for breaching EU competition law on cartels (TFEU Art. 101), 1990–2014.]


**Primary steering effect:**
Safeguarding the proper functioning of the Internal Market and enforcing the application of the polluter pays principle.

**Annual revenue estimate**\(^{194}\):

- **EUR 4.5 billion**
- **In % of total EU budget: 3.1%**
- **In % of national contributions: 3.6%**

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Background:
The Court of Justice of the European Union (CJEU) ensures the proper application of EU law in the member states and can, based on legal infringements by member states or breaches against EU competition law by undertakings, impose sanctions. Fines due to law infringements, based on article 260 TFEU, amounted to EUR 49.4 million representing around 1.18% of total fines entered into the budget. Breaches of competition rules, according to articles 101 and 102 TFEU, yielded increasing revenue in recent years. In 2004, Microsoft Corporation was sentenced to pay a historic record sum of EUR 497.2 million as a fine for its abuse of market power. It may seem paradoxical but revenues generated by the EU Court of Justice, a central EU institution, do not formally generate own resources. Instead of being made available to the European Commission, they are currently used to reduce the share of each member state’s GNI contribution. This has been a source of regular contention between the EU institutions and the member states.

Rationale:
It seems counterintuitive that member states currently profit financially from the wrongdoing of other Union countries by reducing their national contribution share. This implies that fines cannot be used as additional revenue for EU programmes, although these proceed eventually ensure the proper implementation of these programmes. Beyond the CJEU’s role as assuring norm conformity and fair competition, EU own resources based on infringement penalties would restore a greater coherence to the EU budget.

Added Value as Green Own Resource:
If properly incorporated into the own resource system, fines could significantly improve budget cohesion and end the contradictory practice of flowing back to member states’ coffers. In the European Parliament, there seems to be considerable support for inclusion of CJEU as genuine own resources. According to a draft report on the MFF revision, proceeds resulting from fines imposed on companies in breach of EU competition law, as well as penalties imposed on member states due to non-compliance with EU legislation, should automatically flow into the EU budget without being exclusively used to curb member states’ national contributions. The report stresses that these surpluses “should be budgeted as extra revenue in the EU budget, with no corresponding adjustment of the GNI contributions.”

EU progress so far:
Fines could be made available to the EU institutions if they were integrated as a proper EU own resource through an ORD. Given the strong position of the Council in the special legislative procedure on the ORD, the proposal may encounter strong opposition from national governments since they benefit from the status quo. Another possibility to prevent fines from simply being used to reduce member states’ contributions is to assign them to a specific purpose by circumventing the budgetary rule of

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196 Legal consideration includes merger control, antitrust and cartel provisions, price-fixing, abuse of dominant market position etc.
198 They are listed under other revenue, since they are not explicitly considered own resources in the current ORD.
non-assignment. In contrast to national budgets, earmarking is generally not possible as a result of the unity and equilibrium principles of the budget, and the constraints stemming from the appropriation ceilings. The financial regulation specifies exceptions to this rule. One such example relates to interest proceeds stemming from the excessive deficit procedure which flow into the European Financial Stability Facility. In the same spirit the financial regulation could be amended in order to include specific provisions on how fines and penalties would be exempt from non-assignment and thus reserving them for specific expenditure purposes. The specific purpose could be debated and could take the form of a special EU fund with a wide potential range of objectives.

3.8.2 SWOT-Analysis for CJEU Fines

The debate of CJEU fines as new own resources can provide food for thought about the scope of potential alternative revenue sources for the future EU budget as well as about issues of budget consistency and coherence. Regrettably, this policy option is often overlooked as a possible candidate. It constitutes however an additional potential and arguably long overdue resource capable of linking the fight against market failures to the European revenue side.

<table>
<thead>
<tr>
<th>STRENGTHS</th>
<th>WEAKNESSES</th>
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<tbody>
<tr>
<td>• Makes the revenue generated by the Court of Justice available to EU institutions</td>
<td>• Uncertainty about stability of the resource</td>
</tr>
<tr>
<td>• Ensures coherence and transparency of the budget</td>
<td></td>
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<tr>
<td>• Stresses the EU’s role as a guardian of the Internal Market</td>
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<table>
<thead>
<tr>
<th>OPPORTUNITIES</th>
<th>THREATS</th>
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<tr>
<td>• High public awareness due to recent litigations against large MNEs</td>
<td>• Inclusion in ORD potentially difficult</td>
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</table>

Possible to circumvent ORD by using exception to the non-assignment rule
3.8.3 Key messages for CJEU Fines

Table 9: Key messages per target group supporting CJEU fines as a Green Own Resource

<table>
<thead>
<tr>
<th>CJEU fines</th>
<th>ECONOMY</th>
<th>SUSTAINABILITY</th>
<th>SOCIAL</th>
<th>EUROPE</th>
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<tbody>
<tr>
<td>Green Community</td>
<td>• Credible market rules</td>
<td>• Credible market rules</td>
<td>• Legal certainty</td>
<td>• David against Goliath</td>
</tr>
<tr>
<td>Citizens</td>
<td>• Credible market rules</td>
<td></td>
<td>• Legal certainty</td>
<td>• David against Goliath</td>
</tr>
<tr>
<td>Local Councillors</td>
<td>• Credible market rules</td>
<td></td>
<td></td>
<td>• Legal certainty</td>
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<tr>
<td>Industry</td>
<td>• Credible market rules</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Member states</td>
<td>• Credible market rules</td>
<td>• Legal certainty</td>
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</table>

**ECONOMY**

*Credible market rules:* “The CJEU is the guardian of a fair and competitive Single Market justifying the inclusion of court fines as EU own resources”

**Target Groups:** *Green community, citizens, local councillors, industry, member states*

Over the past 25 years, fines for companies infringing EU antitrust rules have increased drastically. In the second half of the decade after the year 2000, fines for companies increased by 250% in comparison to the period 2000–2004. With respect to the second half of the 1990s, fines have even increased by a factor of almost 30 within 10 years\(^2\). This development not only underlines the increasing revenue potential, but also the growing importance of Court rulings in the European market.

**SUSTAINABILITY**

*Legal certainty:* “CJEU judgments ensure the respect and implementation of EU laws and market rules”

**Target Groups:** *Green community, industry*

Every market needs rules in order to function sustainably. The CJEU is a crucial institution guaranteeing that European norms are respected and European member states’ pledges implemented on the ground. The CJEU is crucial to defend the credibility of the EU as a whole as a provider of public goods, not only in the field of climate and environment. Making CJEU fines proper sources for EU revenue could give coherence to the EU budget and strengthen the role of the Court as an effective enforcer of European norms.

**SOCIAL**

*David against Goliath:* “CJEU fines can address power abuse by big market players”

**Target Groups:** *Green community, citizens, local councillors*

Breaches in competition law can be harmful to entire business or industry sectors. The recent case of the Apple sentence corroborates the need to withdraw the possibility of exploiting their advantageous position from dominant market leaders. The European Commission has revealed that in 2014, Apple paid an effective corporate tax

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rate of just 0.005%\textsuperscript{202}. Including Court fines into the own resource system could strengthen the symbolic importance of EU regulation in ensuring fairness and social justice against economic actors that abuse their dominant market position.

\textbf{EU budget consistency:} “CJEU judgements protect EU public goods. Respective revenues should feed into European projects”

\textit{Target Groups:} Green community, citizens, member states

Since fines are not added as additional revenue, they do not increase the overall budget, but are included in the calculations determining the size of member states’ GNI contributions for the upcoming financial year. This implies that a part of the penalty payments paid by member states judged to be in breach of EU competition law virtually flow back to the respective countries in form of reductions of their GNI-based resources. The current state of play – that member states financially benefit from the EU’s efforts to address market manipulations without leaving the EU any scope for own resources derived from these imposed sanctions – is counterintuitive and unacceptable.

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### Overview table with key messages per target group

<table>
<thead>
<tr>
<th>TARGET GROUP</th>
<th>GREEN OWN RESOURCE CANDIDATES</th>
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<tbody>
<tr>
<td></td>
<td>EU Carbon Tax</td>
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<tr>
<td>Green Community</td>
<td></td>
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<td></td>
<td>Decarbonisation</td>
</tr>
<tr>
<td>Citizens</td>
<td>Carbon Bubble</td>
</tr>
<tr>
<td>Local Councillors</td>
<td>Carbon Bubble</td>
</tr>
</tbody>
</table>

- Decarbonisation
- Carbon Bubble
- Low-carbon leakage
- Non-ETS GHGe reductions
- Policy coherence
- Tax shift
- Effort-Sharing
- Support EU ETS
- Level the global playing field
- Making trade greener and fairer
- Effort-Sharing
- Paris-consistent global trade
- Affordable energy transition
- Fairer energy market
- A Paris-consistent path for renewables
- Tax recycling for progressive distribution
- Integrated budget for energy transition
- Towards a Green Energy Union
- Efficient transport market
- Low-carbon mobility
- Low-carbon transport transition
- End tax advantage for diesel
- Improve air quality
- Social effects
- Sustainable mobility
- Fair transport competition
- Improve aviation’s environmental footprint
- Incentivise use of sustainable fuel
- Progressive tax on flying
- Sustainable transport agenda
- Collective action necessary
- Financial market stability
- Circumvent VAT exemption
- Sustainable finance for sustainable markets
- Fair and substantial
- Borderless market
- Reduce tax competition
- Empower SMEs
- Sustaining corporate tax income
- Towards tax justice
- United against tax avoidance
- Credible market rules
- Legal certainty
- David against Goliath
- EU budget consistency
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- Fairer energy market
- Towards more energy independence
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- Integrated budget for energy transition
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- Low-carbon transport transition
- Improve air quality
- Social effects
- Sufficiency
- Fair transport competition
- Improve aviation’s
- Financial market stability
- Circumvent VAT exemption
- Reduce tax competition
- Empower SMEs
- Credible market rules
- Legal certainty
- David against Goliath
- EU budget consistency
<table>
<thead>
<tr>
<th>Local Councillors</th>
<th>Industry</th>
<th>Member states</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Tax shift</td>
<td>• Decarbonisation</td>
<td>• Decarbonisation</td>
</tr>
<tr>
<td>• Effort-Sharing</td>
<td>• Carbon Bubble</td>
<td>• Carbon bubble</td>
</tr>
<tr>
<td>• Making trade greener and fairer</td>
<td>• Low-carbon technology</td>
<td>• Low-carbon technology</td>
</tr>
<tr>
<td>• Towards more energy independence</td>
<td>• Low-carbon leakage</td>
<td>• Low-carbon leakage</td>
</tr>
<tr>
<td>• Integrated budget for energy transition</td>
<td>• Non-ETS GHGe reductions</td>
<td>• Non-ETS GHGe reductions</td>
</tr>
<tr>
<td>• Environmental footprint</td>
<td>• Tax shift</td>
<td>• Policy coherence</td>
</tr>
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**Key Themes:**
- **Economy**
- **Sustainability**
- **Social**
- **Europe**
Conclusion: spreading the word of Green Own Resources

This report is meant to provide food for thought on improving the communication of potential sustainability-enhancing own resource candidates, Green Own Resources, and to open a debate on alternative and greener sources of future EU revenue.

After providing a short overview of the current financing system of the Union and its deficiencies, the main barriers for communicating Green Own Resources were explored. The main part of the study looked into eight specific Green Own Resources and developed arguments in favour of these instruments tailoring them to five specific target groups. These can provide policymakers and supporters of Green Own Resources with an inventory of arguments stressing the added value of aligning the EU financing system with sustainable development objectives.

Obviously, the evaluation presented in this study is far from exhaustive. Each instrument has its own particular strengths and weaknesses, and undoubtedly its own context-specific features whose adequate discussion would go beyond the scope of this study.

2016 is a crucial year for launching discussions on alternative proposals for ambitious future EU own resources. By the end of the year, the HLGOR will present its final report including recommendations on the future financing of the EU budget. This is the time for proponents of Green Own Resources to become active.
References


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Núñez Ferrer et al. (2016). Study on the potential and limitations of reforming the financing of the EU budget. *Study* commissioned by the European Commission on behalf of the High Level Group on Own Resources.


Glossary

A

Appropriations
Term referring to budget funding. Appropriations come in two forms:

Commitments: Legal assurance to grant financial transfer if certain conditions are met.

Payments: Actual cash or bank transfers to beneficiaries.

Aggressive Tax Planning
Legal corporate practice taking advantage of the technicalities of a tax system or of mismatches between two or more tax systems for the purpose of reducing tax liability. It may result in double deductions (e.g. the same cost is deducted both in the state of source and residence) and double non-taxation (e.g. income which is not taxed in the source state is exempt in the state of residence).

B

Backlog or Payment backlog
Notion referring to outstanding payments at the end of the financial year which are carried over to the next year. There are two types of backlogs: ‘Normal’ and ‘abnormal’ backlogs. ‘Normal backlogs’ relate to outstanding payments which are considered unavoidable (such as those stemming from payment claims not paid because they were transmitted in the very last days of the year or those payment claims which are interrupted/suspended for certain beneficiaries). Backlogs are deemed ‘abnormal’ on the other hand when payments at year-end remained unpaid because authorised payment appropriations on the relevant budget line were exhausted.

Base erosion and profit shifting (BEPS)
Refers to tax avoidance strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations.

Budgetary authority
Term referring to the European Parliament and the Council of the European Union which jointly form the EU’s primary legislative authority in overseeing and adopting the annual budget.

C

Call rate
Percentage used as a basis for calculating national contributions to the budget.

E

Enhanced cooperation
Refers to a procedure where a minimum of 9 EU countries are allowed to establish advanced integration or cooperation in an area within EU structures but without the other EU countries being involved under article 20 TEU.

European Single Market or Internal Market
Refers to the European Union’s internal market characterised by the abolition of internal borders and the protection and promotion of the free circulation of people, goods, services and capital, the so-called ‘Four Freedoms’.

G

Gender Budgeting
Term referring to the application of gender mainstreaming to the budgetary process. It means a gender-based assessment of budgets, incorporating a gender perspective at all levels of the budgetary process and restructuring revenues and expenditures in order to promote gender equality.

GNI-based own resource
Currently, the largest of the European Union’s own resources as defined in the ORD according to its share in total revenue accounting to 72.9%. It is based on de facto national contributions based on a uniform call rate which is applied on the member
states’ gross national income (GNI) after corrections have been accounted for. The GNI-based own resource is also referred to as the ‘residual resource’ since it is used to finance the remainder of the EU revenue after all other revenue is calculated and added to the EU budget.

**Green Own Resource**

Potential future own resource of the EU budget with a clear sustainability-oriented steering effect.

**Multiannual Financial Framework (MFF)**

The Multiannual Financial Framework (MFF) ensures a mid-term outlook on financial programming and budgetary discipline for a period of at least five years with the current MFF covering a period of seven years, 2014-2020. It is adopted through a Council Regulation and defines overall spending ceilings for each of the years covered as well as financial specifications for each budgetary heading which cover the EU’s policy fields. The current MFF sets a maximum amount of EUR 960 billion for commitment appropriations and EUR 908 billion for payment appropriations and divides expenditure along six main categories or headings: Smart and Inclusive Growth, Sustainable Growth: Natural Resources, Security and citizenship, Global Europe, Administration and Compensations.

**Own-Resource Decision (ORD)**

Legislative act adopted under a special legislative procedure based on article 311 TFEU defining and establishing and defining a system of own resources for the European Union. ORDs are adopted unanimously in the Council with the European Parliament being consulted and enters into force after all EU member states have approved the decision in line with their “constitutional requirements.”

**Paris Agreement**

Refers to an international climate agreement negotiated under the auspices of the United Nations Framework Convention on Climate Change (UNFCCC) and adopted on 12 December 2015 in Paris. The agreement sets out a peer review process aiming to mitigate greenhouse gas emissions and financially support global transitions towards low-carbon emissions and climate resilience.

**Reste-à-liquider (RAL)**

Notion referring to all outstanding commitments that remain unpaid at a given point in time.

**Tax avoidance**

Legal corporate practice to minimise the amount of tax payable by means within the law.

**Tax evasion**

Illegal practice where a person, organization or corporation intentionally avoids paying his true tax liability. Those caught evading taxes are generally subject to criminal charges and substantial penalties.

**Traditional own resource (TOR)**

Currently, one of the European Union’s own resources as defined in the ORD accounting for 12.9% of total revenue in 2016. They are based on proceeds from customs duties, agricultural duties, and sugar and isoglucose imposed on economic operators and are usually perceived as the most genuine of all current own resources of the EU. Yet, their share has decreased significantly over time.

**VAT-based own resource**

Currently, one of the European Union’s own resources as defined in the ORD accounting for
13.1% of total revenue in 2016. They are de facto national contributions based on a statistical VAT base which is harmonised across member states. Due to its complex calculation and its non-genuine character, it has been proposed to remove the VAT-based resource.
## Annexes

### Annex I: Development of EU budget revenue 1970-2016

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<th>GNI-based</th>
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<th>UK correction</th>
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**Source:**

- **For 1970-2008:**

- **For 2009-2014:**

- **For 2015-2016:**
Annex II: Sequential calculation of the EU budget

Figure 11: Sequential calculation of the EU budget

Note: Own illustration.
Annex III: Policy options for compensatory measures

Figure 12: Policy options to avoid negative distributional effects of ETR on private households

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<td>Energy tax reductions for public transport (Germany)</td>
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<td>Progressive taxation (according to energy consumed)</td>
<td>Progressive electricity tax (GBG, 2008)</td>
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<td>Progressive water/wastewater charges (Portugal)</td>
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<td>Tax-free basic amounts of consumption</td>
<td>Electricity tax in the Netherlands</td>
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<td>Select a tax base that affects richer households more</td>
<td>Taxes or charges applied on air traffic (Leipprand et al., 2007)</td>
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<td>Swiss CO₂ tax Herlitzius and Schick (2008)</td>
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<td>Income tax reductions/income tax reform</td>
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<td>Germany (Bach et al., 2001)</td>
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<td>General support measures for vulnerable households (increase in transfer payments)</td>
<td>GBG (2008)</td>
</tr>
<tr>
<td>Specific support measures for vulnerable households: transfer payments to cover energy costs</td>
<td>Means-tested benefit for heating costs (Germany)</td>
</tr>
<tr>
<td>Specific environment-oriented support measures: subsidies for energy-saving investments, public transport etc.</td>
<td>Subsidies for replacement of night storage heating (Germany)</td>
</tr>
<tr>
<td></td>
<td>Netherlands until 2003</td>
</tr>
<tr>
<td></td>
<td>GBG (2008)</td>
</tr>
<tr>
<td></td>
<td>Ekins and Dresner (2004)</td>
</tr>
<tr>
<td></td>
<td>McNally and Mabey (1999)</td>
</tr>
</tbody>
</table>

Annex IV: EU Air Ticket Tax – list of countries with existing and abolished air ticket tax

<table>
<thead>
<tr>
<th>Country</th>
<th>Denomination</th>
<th>Rates for short; medium; long haul; economy/business</th>
<th>Tax revenues in Mio. € (in % of GDP)</th>
<th>Introduced in</th>
<th>Modifications</th>
</tr>
</thead>
<tbody>
<tr>
<td>Norway</td>
<td>Passenger Tax</td>
<td>128.6 NOX (15.90 €)</td>
<td>173 (0.09)</td>
<td>1978</td>
<td>Introduced as charter traffic tax in 1978, modified to passenger tax in 1994 and decreased, modified to seat tax in 1998 and decreased, modified to passenger tax in 2001. Abolished in 2002</td>
</tr>
<tr>
<td>Malta</td>
<td>Departure Tax</td>
<td>120</td>
<td>6 (0.06)</td>
<td>2001</td>
<td>Abolished in 2008</td>
</tr>
<tr>
<td>Denmark</td>
<td>Passagerafgift (Air Passenger Duty)</td>
<td>75/300 DKK (10.07/40.26 €)</td>
<td>45 (0.02)</td>
<td>2005</td>
<td>Halved in 2006. Abolished in 2007</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>Vliegbelasting (Air Passenger Duty)</td>
<td>11.25/11.25; 11.25/11.25; 45/45</td>
<td>19 (0.003)</td>
<td>2008</td>
<td>Abolished in 2009</td>
</tr>
<tr>
<td>Ireland</td>
<td>Air Travel Tax</td>
<td>3/3; 3/3; 3/3</td>
<td>24 (0.02)</td>
<td>2009</td>
<td>Reduced in 2011. Abolished in 2014</td>
</tr>
</tbody>
</table>

Existing ticket taxes

<table>
<thead>
<tr>
<th>Country</th>
<th>Denomination</th>
<th>Rates for short; medium; long haul; economy/business</th>
<th>Tax revenues in Mio. € (in % of GDP)</th>
<th>Introduced in</th>
<th>Modifications</th>
</tr>
</thead>
<tbody>
<tr>
<td>France</td>
<td>Taxe de l'aviation civile (Civil Aviation Tax)</td>
<td>4.36/7.85³</td>
<td>76 (0.004)¹</td>
<td>1999</td>
<td>Indexation to CPI since 2011. Increased in 2014. Introduction of a rebate of 50% for transit passengers in 2015. Introduction of a rebate of 100% for transit passengers in 2016.</td>
</tr>
<tr>
<td></td>
<td>Taxe de solidarité sur les billets d'avion (Solidarity Levy)</td>
<td>1.13/11.27; 4.51/45.07</td>
<td>204 (0.001)¹</td>
<td>2006</td>
<td></td>
</tr>
<tr>
<td>Austria</td>
<td>Departure Tax (Flugticketabgabe)</td>
<td>7/7; 15/15; 35/35</td>
<td>109 (0.02)¹</td>
<td>2011</td>
<td>Reduced in 2013</td>
</tr>
<tr>
<td>Germany</td>
<td>Departure Tax (Luftverkehrsteuer)</td>
<td>7.30/7.50; 22.43/22.43; 42.18/42.18</td>
<td>988 (0.03)¹</td>
<td>2011</td>
<td>Reduced in 2012</td>
</tr>
<tr>
<td>Bosnia &amp; Herzegovina</td>
<td>Departure Tax</td>
<td>16.81</td>
<td>n.a.</td>
<td>n.a.</td>
<td></td>
</tr>
<tr>
<td>Croatia</td>
<td>Civil Aviation Tax</td>
<td>0.68/1.37⁹</td>
<td>n.a.</td>
<td>n.a.</td>
<td></td>
</tr>
</tbody>
</table>

## Annex V: Exceptions to the non-assignment rule

<table>
<thead>
<tr>
<th>External assigned revenue</th>
<th>Internal assigned revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Financial contributions from member states to certain research programmes pursuant to the Council Regulation implementing the Decision on the system of the Communities’ own resources,; the reason for this is because not all member states take part in the programmes concerned</td>
<td>• Revenue from third parties in respect of goods, services or work supplied at their request</td>
</tr>
<tr>
<td>• Financial contributions from member states and third countries, including in both cases their public agencies, entities or natural persons, to certain external aid projects or programmes financed by the Union and managed by the Commission on their behalf</td>
<td>• Proceeds from the sale of vehicles, equipment, installations, materials and scientific and technical apparatus which are being replaced or scrapped when the book value is fully depreciated</td>
</tr>
<tr>
<td>• Interest on deposits and the fines provided for in the Regulation on speeding up and clarifying the implementation of the excessive deficit procedure</td>
<td>• Revenues arising from the repayment of amounts wrongly paid</td>
</tr>
<tr>
<td>• Revenue earmarked for a specific purpose, such as income from foundations, subsidies, gifts and bequests, including the earmarked revenue specific to each institution</td>
<td>• Proceeds from the supply of goods, services and works for other departments within an institution, institutions or bodies, including refunds by other institutions or bodies of mission allowances paid on their behalf</td>
</tr>
<tr>
<td>• Financial contributions to Union activities from third countries or from non-Union bodies</td>
<td>• Insurance payments received</td>
</tr>
<tr>
<td>• Revenue generated by the Research Fund for Coal and Steel</td>
<td>• Revenue from payments connected with lettings</td>
</tr>
<tr>
<td>• Revenue generated by the activities of the Joint Research Centre</td>
<td>• Revenue from the sale of publications and films, including those on an electronic medium</td>
</tr>
<tr>
<td>• Internal assigned revenue ancillary to any of the above</td>
<td>• Repayments to financial instruments</td>
</tr>
<tr>
<td></td>
<td>• Revenue arising from reimbursement of taxes by third countries</td>
</tr>
<tr>
<td></td>
<td>• Revenue stemming from a basic act adopted laying down the basis for a Union programme unless otherwise provided (article 21(4))</td>
</tr>
</tbody>
</table>

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### Source


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203 Contributions from Third Countries are calculated by applying a ‘proportionality factor’ relating to the GDP ratio of the Union member states and that of the third country in question. Such contributions are not included in the budget, but appear in an Annex to the budget ‘for information’ only. Likewise can contributions by candidate countries be calculated and assigned to the budget while their ultimate contributions are defined on a case-by-case basis in the association councils.