

Plugging the fiscal black hole: transport's revenue raising potential

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Summary

The transport system is not paying its fair share of tax at a time when the nation's finances are under severe pressure. Transport tax reform could help to rebuild rather than compound the government's financial challenges. We have modelled reforms that have the potential to generate additional revenues of £23 billion in 2030 and £34 billion in 2035, all while pursuing the urgent need to incentivise lower carbon travel. In this briefing we also identify those road building projects which are poor value for money and so should be scrapped in favour of alternative high value investments.

Transport tax needs to change

The transport system has long been a significant contributor to the exchequer, but revenues are being eroded. In 2022-23, fuel duty, the single biggest transport tax, raised over £25 billion, equivalent to Ministry of Defence spending on UK industry in 2022-23.^{1,2} The Office for Budget Responsibility (OBR) notes, however, that the effective rate has fallen in real terms, in part due to decisions by successive governments to freeze or cut rates since 2011, and the increasing number of drivers switching to electric vehicles (EVs).³ The OBR's latest forecast shows that fuel duty and vehicle excise duty (VED) receipts will only contribute 0.3 per cent of GDP in the latter half of this century, four times lower than today.⁴

Transport is also not paying its fair share for the emissions it generates. Aviation, for example, is a significant polluter, producing 32 million tonnes of carbon dioxide equivalent (MtCO₂e) in 2023, second only in the transport system to the emissions from the UK's entire car fleet.⁵ Despite this impact, commercial aviation does not pay fuel duty and VAT, unlike the nation's drivers. Revenue raising from aviation is limited to Air Passenger Duty (APD), a distance banded charge on ticket purchases, and the Emissions Trading

Scheme (ETS).⁶ These are predicted to bring in 0.2 and 0.1 per cent of national income respectively during 2024-25 compared to 0.9 per cent raised from fuel duty.⁷

How to raise £34 billion by 2035

Below, we outline a range of transport taxes, modelled by WPI Economics on behalf of Green Alliance. The figures show the significant revenues that could be raised by 2035:⁸

- £23.5 billion for a comprehensive road pricing scheme
- £8.5 billion by appropriately pricing aviation jet fuel
- £1.7 billion from a shipping fuel levy

The road pricing element has been costed such a way to cover falling fuel duty receipts while incentivising lower annual mileages and the use of zero emission vehicles. Kerosene tax and shipping fuel levy rates ramp up from 2025, reaching a level consistent with the government's carbon value in 2035. This allows for a period of adjustment for industry and consumers while introducing policy levers necessary to tackle climate impacts.

For full rates, revenues and emissions impact details see the annex at the end of this briefing.

Reforming existing taxes

Uprating existing taxes may be more politically feasible than introducing road pricing. However, taxes would need to be increased significantly to maintain revenues. For example, a 25 pence per litre increase in fuel duty by 2030, on top of the ending of the five pence temporary cut introduced in 2022, would raise almost £7 billion and cut 1.7 MtCO₂e per annum.

In aviation, the Treasury could choose to generate additional revenue and cut emissions via APD. To raise an additional £2 billion a year by 2030, APD would need to increase by 50 per cent. This rise would reduce emissions by 3.4 MtCO₂e a year.

These approaches are limited as they are less able to account for changing technologies. A kerosene tax, for example, can be appropriately discounted to encourage the use of Sustainable Aviation Fuels and zero emission flight technologies, whereas this is more challenging for a ticket tax like APD.

Fuel duty charges need to increase substantially to avoid revenues continuing to fall as the EV transition ramps up. At present, EVs tend to be driven by wealthier households. While upfront prices are coming down and the second hand market provides a more affordable way to purchase an EV, cars continue

to be used for longer. An inequality challenge will remain if no alternative to fuel duty is found, and drivers of older petrol and diesel vehicles pay higher rates.

Ensuring taxes are fair

It is crucial that fairness is embedded in reform. Forms of transport with a particularly high social or environmental impact should be taxed proportionately if broader tax changes are to take place.

Private jets, for example, are the single biggest generator of per passenger emissions and should, therefore, be taxed higher than commercial flights. A £1 per litre tax applied to 2022 private jet fuel would have generated £200 million for the Treasury.⁹ Inequality is still a feature of commercial aviation, as around half of UK people do not fly and many take just one return flight per year. The Treasury should commission work into the implementation and appropriate pricing of a frequent flyer levy to reflect the much higher environmental impact of regular flyers.

Larger and heavier cars also are also less energy efficient, increase road damage, cause higher air pollution and are a bigger danger to pedestrians, cyclists and other road users than smaller models. Adjusting VED according to vehicle weight to encourage the development of smaller, more affordable EVs should also be investigated.

Reprioritising road spending

The Department for Transport (DfT) was recently given the worst grade by the National Audit Office for its delivery of spending to act on climate change.¹⁰ Expanding the UK's Strategic Road Network (SRN) with new projects has low returns for public money spent. Spending could be more productively redirected towards a programme of maintenance of, and investment in, public transport and active travel infrastructure, in support of the government's growth mission. Constructing new roads increases greenhouse gas emissions, from the production of the materials used in construction and the greater vehicle use induced by increased road capacity.¹¹

As the government sets the portfolio for the Road Investment Strategy 3 (2025-30), initially assessed to cost £11.5 billion, it should reallocate spending from large scale road projects where the economic case is weak, to projects with better returns on investment.¹²

Lower Thames Crossing

A development consent order decision is due to be taken on the Lower Thames Crossing by 4 October. The scheme is anticipated to cost at least £9 billion, though delays will continue to drive up the cost of this scheme, which is

already more expensive per mile than HS2.¹³ Moreover, the returns on this investment, represent poor value for money. The DfT's own assessment suggests a benefit cost ratio (BCR) for the Lower Thames Crossing of 1.46, significantly below comparative investment in active travel infrastructure, with a BCR of 5.6.^{14,15}

Cancelling the Lower Thames Crossing, for instance, could lead to a potential £9 billion saving for the government, or an additional investment stream to be redirected to support the government's growth and health missions.

Recommendations

The government should:

- Set up an independent commission to design an equitable road pricing scheme to replace fuel duty.
- In the short term, end the 2022 cut to fuel duty and lift the fuel duty freeze, allowing rates to rise in line with inflation.
- Introduce a kerosene tax at 9p per litre in 2025, then ramp it up annually to reach 97p per litre in 2035 for all flights, where air service agreements allow.
- Redirect funding for large scale road projects with weak economic cases, including the Lower Thames Crossing, to lower carbon transport infrastructure.

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Endnotes

¹ Office for Budget Responsibility (OBR), April 2024, 'Fuel duties'

² Ministry of Defence (MOD), 8 February 2024, 'MOD regional expenditure with industry 2022/23'

³ OBR, 'Fuel duties', op cit

⁴ OBR, September 2024, *Fiscal risks and sustainability*

⁵ M Finch, April 2024, 'Above the clouds: UK aviation trends in 2023', Transport & Environment briefing

⁶ Ibid

⁷ OBR, April 2024, 'Air passenger duty'; and 'Emissions trading scheme (UK ETS)' April 2024

⁸ For a full explanation of suggested tax changes across road, aviation and shipping see: S Dossett and J Beckford, June 2023, *Reforming transport taxes: a fair share package*

⁹ H Bennett, July 2023, 'Taxing private jets: raising revenue from highly polluting, luxury aviation', Green Alliance briefing.

¹⁰ National Audit Office, 2023, *Department for Transport (DfT) departmental overview*

¹¹ L Hopkinson and P Goodwin, 2023, 'Induced traffic: yet again a worryingly overlooked dimension in crucial road planning and appraisal policy', TAPAS.network

¹² Department for Transport (DfT) and National Highways, November 2022, *Road enhancements: progress with the second road investment strategy (2020 to 2025)*

¹³ Green Alliance analysis, finding at around £9 billion for 14 miles, the Lower Thames Crossing will cost over £630 million per mile of road, compared to £396 million per mile of HS2.

¹⁴ Department for Transport, 2023, 'Lower Thames Crossing: accounting officer assessment'

¹⁵ House of Commons, 2020, *Active travel: trends, policy and funding*

Annex

Transport tax rates, revenues and emissions impacts

Tax		2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035
Road pricing reform	Rate (£/litre)*	0.02	0.02	0.02	0.03	0.03	0.03	0.03	0.04	0.04	0.05	0.05
	Revenues (£bn)	10.5	11.8	13.1	14.8	14.2	16.9	17.0	17.2	20.1	20.3	23.5
	Carbon savings (MtCO ₂ e)	-1.3	-1.4	-1.5	-1.6	-1.4	-1.5	-1.4	-1.3	-1.4	-1.3	-1.4
Kerosene taxation	Rate (£/litre)**	0.09	0.18	0.26	0.35	0.44	0.53	0.62	0.71	0.79	0.88	0.97
	Revenues (£bn)	0.8	1.6	2.4	3.2	4.0	4.7	5.5	6.2	7.0	7.8	8.5
	Carbon savings (MtCO ₂ e)	-0.4	-0.7	-1.1	-1.4	-1.8	-2.1	-2.5	-2.9	-3.3	-3.7	-4.1
Shipping fuel levy	Rate (£/metric tonne)	90	181	271	362	452	542	633	723	814	904	994
	Revenues (£bn)	0.4	0.8	1.2	1.6	1.9	2.0	2.2	2.4	2.6	2.7	1.7
	Carbon savings (MtCO ₂ e)	-0.3	-0.6	-0.9	-1.2	-1.5	-3.7	-4.3	-5.0	-5.7	-6.4	-10.7

* In addition to existing taxes and with extra charges for distance travelled over 5,000 miles

** Applied to domestic, EU and US flights