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The Road Haulage Industry: costs and taxes

There is considerable discussion about the costs faced by the road haulage industry and the effect on those costs of government policies. This paper collects together what information is available about fuel duty, road taxes and tolls in this country and the rest of the European Union.

Fiona Poole

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Summary of main points

There is little common ground at present between the estimated costs to the road haulage industry quoted by the government and by the industry. Much depends on the size of the firm and what is compared, how many trucks a firm has and how many people it employs. A forum has been set up of Transport, Trade and Treasury ministers and representatives of the Freight Transport Association (FTA) and the Road Haulage Association (RHA) to consider "the general issues of competitiveness, domestically and internationally of the road haulage industry." One of the prime objectives of the group is to find common ground on the statistics that relate to this.

The position of the road haulage industry is that irreparable damage is being inflicted on their members by the government's transport taxation policies, in particular on fuel and vehicle excise duty (VED). Fuel costs account for up to 35% of all UK haulage costs and so are particularly important to the industry. The industry argues that Britain is the only country in Europe that operates a fuel duty "escalator", raising fuel duty by at least 6% plus the existing level of inflation each year.

The government recognises the industry's concerns about the price of fuel but considers, first, that the fuel escalator is one of the best ways of encouraging fuel efficiency and second, that it is only one factor in haulage costs. It argues that UK hauliers benefit from more favourable company taxation and social costs than in many EU countries.

Despite efforts by the European Union to try to harmonise transport costs for heavy goods vehicles, there are still variations in rates of vehicle excise duty or its equivalent, in fuel duty, road charges and motorway tolls between member states. In 1995 the European Commission published a green paper *Towards fair and efficient pricing in transport* in which it argued that there could be a potential distortion of competition between hauliers of different nationalities. Efforts at producing a European policy are still continuing. It is difficult to compare costs across borders, especially for VED. The Department of the Environment, Transport and the Regions (DETR) is wary of publishing figures for road taxes in particular, as registration systems in member states are so varied. However the FTA has published figures and the European Commission included comparative material in its 1995 green paper.

The impact of company taxes and labour costs on any individual company will depend on the size and type of the company concerned, as much as on individual rates of tax.

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I Introduction

The road haulage industry as a whole is both diverse and fragmented. It ranges from the owner drivers with a single lorry operating on the "tramp" principle, to specialist hauliers of, for example, bulk liquids, to large fleets.

Road freight is the dominant form of transport in the UK domestic market: it accounts for 68% of freight moved (tonne-kilometres) and 83% of total tonnes lifted. 95% of road freight is transported by heavy goods vehicles (i.e. over 3.5 tonnes gross vehicle weight). The total number of heavy lorries on the road has remained broadly static over the past few years. At the end of 1997 there were over 400,000 vehicles over 3.5 tonnes, but with articulated vehicles increasing at the expense of rigid ones. International freight traffic through the Channel tunnel has expanded rapidly since its opening in May 1994.[1]

Efficient distribution of goods and services is vital for economic development: it determines market diversity and consumer choice and has led to less waste with more effective stock management at every point of the supply chain. The DETR estimate that the core activities comprised in logistics (the term used to describe the designing and managing of the supply chain in the wider sense) accounts for nearly 4% of gross output, valued at around £55 billion a year. There are over one million jobs in commercial transport and warehousing activities, accounting for around 3.5% of total employment. The freight transport element of logistics typically accounts for between 5% and 10% of business costs, although this proportion can be considerably higher in some heavy industrial sectors.[2]

Lorries cause damage to roads and bridges and cause congestion; vehicle emissions impact on air quality and public health. The industry is taking measures to reduce noise and pollution and to minimise such things as empty running but road traffic is forecast to increase by at least 38% over the next 20 years.[3] This will bring with it a consequent increase in accidents, pollution, disturbance and congestion, which the government, like its predecessor, is trying to limit. Its taxation measures have proved particularly unpopular with the hauliers, some of whom have staged protests and lobbied Parliament. There is little common ground at present between the costs to the road haulage industry estimated by the government and by the industry itself. There is no simple answer to how much a road haulage firm will pay in taxes and how this compares with its European competitors. Much depends on the size of the firm and what is compared, how many trucks a firm has and how many people it employs. The industry concentrates on the cost of fuel and road tax; the government concentrate on the more favourable company taxation and social costs to companies operating in the UK.

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1 DETR *Focus on freight* August 1998

2 DETR *Sustainable distribution: a strategy* March 1999 para 2.5

3 Department of Transport *National road traffic forecasts: Great Britain 1997* HMSO 1997

A forum has been set up of Transport, Trade and Treasury ministers and representatives of the Freight Transport Association (FTA) and the Road Haulage Association (RHA) to consider "the general issues of competitiveness, domestically and internationally of the road haulage industry." One of the prime objectives of the group is to find common ground on the statistics that relate to this. The first meeting took place on 8 April 1999.

This paper brings together figures on road taxes, fuel duty, corporation tax and labour costs that are publicly available and on which the comparisons seem to have been based. It does not cover other costs, such as operator licence fees, income tax or value added tax which could also be relevant.

II The Costs

A. Lorry Weights

Lorry weights are not a direct cost for the hauliers but recent changes to the maximum lorry weights allowed has had a significant effect, both on the government's recent changes to VED and on future costs to the industry.

Until January 1999 the maximum gross weight for articulated heavy goods vehicles (on 5 or 6 axles) in the UK was 38 tonnes. The maximum drive axle weight for all these vehicles was 10.5 tonnes. In addition since 1994 6 axle articulated vehicles and drawbar-trailer combinations weighing 44 tonnes have been allowed but only when carrying containers for transfer to rail services or for delivery after being conveyed by rail.

Since 1 January 1999 40 tonne, 5 axle lorries have been allowed on UK roads in accordance with European Union rules. At the same time the maximum axle weight for lorries was raised from 10.5 to 11.5 tonnes. Although under EU law, the requirement only applied to international journeys, the government decided it would be difficult in practice to distinguish national from international journeys and so announced in the transport white paper last July that it would allow such vehicles to be used for both domestic and international journeys.[4] The limit for combined road/rail transport continues to be 44 tonnes.

These changes do not alter the size of vehicles but allow more load per vehicle carried. Increases in the maximum load any lorry can take will improve efficiency and competitiveness of the industry but at a cost. Increased axle loading causes greater road and bridge wear. A 40 tonne, 5 axle lorry with 11.5 axle weight causes about a third more wear than the lorries previously permitted. In the transport white paper, the government said it would develop a strategy to provide hauliers with incentives to make greater use of 6 axle lorries instead of 5 axle ones.[5] A 6 axle lorry is less damaging to roads and bridges

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4 DETR *A new deal for transport: better for everyone* July 1998 Cm 3950 para 3.160

5 Ibid, para 3.163

because the extra axle allows the weight to be more evenly spread. However the load a 6 axle lorry can carry is less as the extra axle weighs about a tonne. In addition the vehicles are more expensive, making them less attractive to hauliers.

To encourage hauliers to use 6 axle vehicles, the government announced that it would allow 41 tonne gross weight vehicles on 6 axles on UK roads from 1 January 1999. This means they will carry approximately the same load as a 40 tonne lorry on 5 axles but cause less road and bridge wear because the maximum axle weight will be limited to 10.5 tonnes under UK regulations.[6]

The 1999 Budget introduced a higher rate of VED for this group of vehicles with 11.5 tonne axle weight to discourage their use.

The industry is concerned about these changes and the government's response was put recently by transport minister, Glenda Jackson in response to a PQ:[7]

Goods Vehicles

> **Mr. Wigley**: To ask the Secretary of State for the Environment, Transport and the Regions what steps he is taking to ensure that British haulage operators do not face unfair competition as a result of tax increases proposed on vehicles running at an 11.5 tonne drive axle weight on roads in Britain.
>
> **Ms Glenda Jackson**: As my right hon. Friend the Chancellor of the Exchequer announced in his pre-Budget statement on 3 November 1998, vehicle excise duty rates for goods vehicles with 11.5 tonne axle weights will be set to discourage strongly the use of such vehicles, in view of the additional road damage that they cause. The Integrated Transport White Paper stated that the Government would seek to encourage the use of goods vehicles with a maximum weight of 41 tonnes on 6 axles, which have the same payload as 40 tonnes on 5 axles but cause significantly less road wear.
>
> The Government firmly believe that the best way to help industry, including hauliers, is to create a climate of sustainable economic growth and long-term investment in business. The last Budget included a number of general measures from which hauliers could benefit: main corporation tax will be reduced to 30 per cent. from 1 April 1999, and small companies' corporation tax rate will be cut to 20 per cent. from 1 April 1999.

The government considered allowing 44 tonne 6 axle lorries for general use. This is discussed in more detail in Part III of the paper. In effect these are the same as the existing 38 tonne vehicles in that they are the same size, they meet the same requirements

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[6] Much of the initial consultation on this subject was in response to a consultation paper, *Lorry Weights - a consultation paper* published by the Conservative government in December 1996

[7] PQ HC Deb 16 February 1999 c 599W

as to braking and noise and their effects on road wear are similar. Each lorry fully laden would make fewer journeys for the same distribution tasks. On the other hand it felt that such a move would discourage the switch of freight from road to rail which is one of the key objectives of the white paper. The conclusion was to refer the decision to the proposed Commission for Integrated Transport to be set up to provide the government with independent advice on the implementation of the integrated transport policy.[8] Whatever conclusion the Commission reaches, it is not the government's intention to introduce 44 tonne lorries generally before 2003, to give the railways the chance to develop the heavy load market.

Further discussion of the lorry weights issue, along with the government's detailed proposals following the transport white paper, for measures "to improve the efficiency of lorries and to mitigate their effects on the community and the environment" are set out in its paper on sustainable development.[9]

B. Vehicle Excise Duty

1. United Kingdom

If a road haulier has a vehicle registered in the UK, he will be paying vehicle excise duty (also known as road tax) which varies according to the vehicle's axle weight. Under the 1949 Geneva Convention which was superseded by the Vienna Convention of 1968, if a vehicle is licensed in its own country it is entitled to operate abroad.

The Chancellor of the Exchequer announced a review of the basis of VED rates at the time of the 1998 budget.[10] This included a review of the system for setting VED rates for lorries. The intention is to ensure that environmental damage, including to roads, caused by different types of lorries is reflected in their VED rates. No report has yet been published on this although a consultation paper has been published on the options for reforming VED on cars.[11] The transport white paper included the following paragraph:[12]

> 4.126 The Chancellor has already announced that he will review the system for setting VED rates for lorries to ensure that the environmental damage they cause is reflected in their VED rates. This review will take into account the wider environmental impacts of lorries as well as their physical effects on the road infrastructure. The present system does not, for example, take axle loading, which has a substantial effect on road wear, properly into account. With the introduction of new lorry weights .. it will be particularly important to ensure that those operating vehicles with 11.5 tonne maximum axle weight pay a rate of VED

8 Op cit, *A new deal for transport* para 3.168
9 Op cit, *Sustainable distribution* pp 72-4
10 HC Deb 17 March 1998 c 1109
11 HM Treasury *Consultation on reform of VED to ensure a cleaner environment*, November 1998
12 Op cit, *New deal for transport* para 4.126

> commensurate with their increased road costs in comparison to vehicles operating at a maximum of 10.5 tonnes. This review will therefore consider the VED rates for these new lorry weights.

The Chancellor announced in his 1998 Budget a freeze on the VED rate for lorries until the new graduated VED had been devised and also a reduced VED rate by up to £500 from 1 January 1999 for lorries and buses meeting low emission standards.[13] The 1999 Budget continued the freeze on most lorry VED rates and doubled to £1,000 the maximum discount for low emission lorries and buses.[14] Under this scheme, vehicles adapted to meet strict emissions standards will obtain a reduced pollution certificate that will reduce their vehicle excise duty by up to £1000 a year. There are two ways in which the standards are likely to be achieved: by re-engining the vehicle to a higher environmental standard - including conversion to run on alternative fuels such as LPG or CNG - or by fitting a device that reduces particulate emissions. The government believes that the scheme will encourage operators of lorries and buses to improve the environmental performance of their vehicles.

The VED payable from 10 March 1999 for a selection of vehicles is set out in the Budget press notice.[15] Despite a general freeze on rates, the rates for the new classes of heavy lorries first allowed on the roads on 1 January 1999 are increased as promised "to discourage strongly the use of vehicles with 11½ tonne axle weights, in view of the additional road damage that they cause." To encourage combined transport operations i.e. those where freight is transported by road and rail, the VED for vehicles engaged on this work is set at £1,280, a decrease of £1,500 for some vehicles.

There are so many variations that it is difficult to single out particular VED rates but perhaps the following three should be noted:

- 38 tonne vehicles on 5 axles (axle weight 10.5), the most common size of large lorry in the UK and until January 1999 the maximum allowed: VED £3,210

- 40 tonne vehicles on 5 axles (axle weight 11.5), the size now allowed as a result of the EU directive and the group the government wish to discourage: VED £5,750

- 41 tonne vehicles on 6 axles (axle weight 10.5): VED £2,500

The amount of revenue raised from VED on heavy goods vehicles from May 1997 to September 1998 was £818 million.[16]

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13 Introduced under section 10 and schedule 1 of the *Finance Act 1998*
14 HC Deb 9 March 1999 c 181
15 HM Treasury Budget press notice 7, 9 March 1999 "Reform of VED to protect the environment"
16 PQ HC Deb 17 November 1998 c 549W

2. Rates in the EU

Rates in the EU Comparison of VED rates or the equivalent in the EU is not straightforward. In response to a PQ from Bernard Jenkin, the government said: "VED in other member states is based on a variety of different factors such as types of fuel, power output, weight and noise. It is thus, impossible to make direct comparisons across the EU member states."[17] A table in *Motor Vehicle Taxation in Europe* showed how rates could be based on a variety of factors such as deadweight, laden weight, axles, fuel and pollution in different states.[18] At the present time of writing there are a number of PQs down asking for a comparison of VED rates and the DETR is trying to compile a meaningful table. The problem of any comparison is not only to distinguish the different systems of registration but also to recognise the importance of the rate of exchange.

Nevertheless, two organisations have collated figures. The European Commission's 1995 green paper, *Towards Fair and Efficient Pricing in Transport* attached figures, in ECUs, to the rates in different states:[19]

Table 4 — *Road taxes applied in the European Union (ECU)*

Member state	**Annual vehicle tax[1]**
Belgium	940[2]
Denmark	1,245
Germany	2,676
Greece	307[3]
Spain	464[3]
France	787
Ireland	1,965
Italy	711
Luxembourg	779
Netherlands	1,038
Austria	2,825
Portugal	349[4]
Finland	3,333
Sweden	2,591
UK	4,100
EU legislation (minimum)	700

[1] HGV 38 tonne (1994), [2] HGV 40 tonne (1994), [3] Greece, Spain and Portugal are allowed lower rates until 1.1.1997.

Source: Commission services

[17] HC Deb 9 November 1998 c 103W

[18] European Automobile Manufacturers Association *Motor vehicle taxation in Europe* 1995 p 9

[19] COM (95) 691 final 20.12.95

The Commission's figures are now quite old. The FTA published rates for 1998 in the joint FTA/RHA submission on the 1999 Budget.[20] These were obtained by contacting the trade associations in the different countries and asking for a typical rate for a 40 tonne vehicle:

VED rates in 15 EU Member States as at December 1998 for a 40te gvw (2+3) articulated vehicle

	VED (£)
Austria	2,123
Belgium	929
Denmark	498
Eire	1,384
Finland	1,084
France	486
Germany	1,856
Greece	428
Italy	634
Luxembourg	358
Netherlands	670
Portugal	308
Spain	328
Sweden	1,909
UK	3,210*

Source: FTA *rate for 38 te gvw (2+3)

It should be stressed how difficult it is to obtain accurate and meaningful comparisons. For example, the figure for France, quoted above as £486 and frequently used in press reports, was apparently given as £660 to the DETR by the official French road haulage body. Comparisons will also be affected by the exchange rate.

The Chancellor was asked in June 1998 what plans he had to bring vehicle excise duty into line with average levels in EU countries and the reply was "none".[21]

The Chancellor was also asked what assessment he had made of the impact on the competitiveness of the UK road haulage industry of differences in VED and excise duty on diesel. Ms Hewitt, on his behalf, replied that the impact on competitiveness was one of the factors that the Chancellor took into account when making decisions on the budget.[22]

20 FTA/RHA joint Budget submission 1999
21 PQ HC Deb 23 June 1998 cc 451-2W
22 PQ HC Deb 17 November 1998 c 549

C. Fuel Duties

In the UK, pre-tax prices are below the EU average. The highest rate of duty in the Union, however, makes UK pump prices the most expensive.

The government has introduced two important changes in the taxation of road fuels since May 1997 and both affect road hauliers:

- Road fuel duties are to be increased by at least 6% in real terms each year. The Conservative government introduced a "road fuel escalator" (the commitment to increase duty rates by a specified percentage each year) in the March 1993 Budget. Initially this was set at 3% in real terms, though it was increased to 5% in the November 1993 Budget. The Chancellor, Gordon Brown, announced a further 1 percentage point increase in his July 1997 Budget.[23]

- The rate of duty on road diesel is to be increased steadily, *relative* to the rate of duty on unleaded petrol. In the November 1994 Budget the duty on petrol was set at 35.26p per litre, and the duty on road diesel at 30.44 per litre - the same rate of duty as on unleaded petrol. This 5 pence differential between the rate on petrol, and that on diesel & unleaded petrol, was maintained until the March 1998 Budget. The Chancellor then announced that the duty on diesel would be increased by an additional 1 pence per litre, relative to the duty on unleaded petrol. This was the first step in a longer term strategy, to tax petrol and diesel more fairly, based on the energy and carbon content - so that the duty on diesel will be raised to a level above that of petrol.[24]

The 1999 Budget increased the duty on ordinary diesel by 6.14p a litre (new rate 50.21p a litre or 228.26p per gallon) although the duty on ultra low sulphur diesel (ULSD) rose by only 4.96p (new rate 47.21 a litre or 214.62p per gallon). The intention is that all diesel will be replaced by ULSD by 2000.

The environmental effects of the escalator were set out in a PQ in February 1999 as follows:[25]

> **Dr. Marek**: To ask the Chancellor of the Exchequer if he will publish the Treasury's environmental appraisal on the effects of the policy to increase fuel duty by six per cent per annum in real terms.
>
> **Ms Hewitt** *[holding answer 22 February 1999]:* The Pre-Budget Report, published on 3 November 1998, included an environmental assessment of the Government's environmental tax measures to date. The road fuel duty escalator,

[23] HC Deb 2 July 1997 c 311
[24] HC Deb 17 March 1998 c 1110
[25] PQ HC Deb 25 February 1999 c 426W

> over the period 1996 to 2002, is estimated to reduce annual carbon dioxide emissions by between 2 million and 5 million tonnes of carbon in 2010. It is also estimated that the 2010 urban road transport emissions of oxides of nitrogen and particulate matter will be reduced by 1 per cent and 1.2 per cent respectively.

The financial effects of the escalator were set out in response to a PQ from John Whittingdale:[26]

> **Mr. Whittingdale:** To ask the Chancellor of the Exchequer how much extra revenue will be raised in excise duty on *(a)* diesel and *(b)* ultra-low sulphur diesel due to changes made since 1 May 1997 in 1997-98 and each of the following four years.
>
> **Dawn Primarolo:** HM Customs and Excise estimate the extra revenue raised in excise duty on *(a)* diesel and *(b)* ultra-low sulphur diesel due to the changes made since 1 May 1997 to be:

		£ m
Financial year	*Diesel*	*Ultra-low sulphur diesel*
1997-98	220	-5
1998-99	570	10
1999-2000	120	430
2000-01	0	900
2001-02	0	1,040

> The figures have been calculated by comparing estimated revenue streams under the current Government's duty commitments (as shown in table C. I of the 1998 FSBR and table IB.2 of the 1999 ESBR/FSBR) with an estimate of what revenue streams would have been under the previous Government's 5 per cent. escalator. It has been assumed that after 1999-2000 all diesel will have been replaced with ultra-low sulphur diesel.
>
> Although it was legislated for under the previous Government, the separate rate for ultra-low sulphur diesel did not come into effect until after 1 May 1997 and has therefore been treated as a change since that date.

According to another PQ it is not possible to separate the revenue raised from excise duty on diesel paid by the road haulage industry from the total revenue received.[27]

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[26] PQ HC Deb 19 March 1999 c 861W
[27] PQ HC Deb 17 November 1998 c 549W

The following table shows diesel prices and the fuel duty rates and taxes across the EU.[28]

Diesel Prices and Taxes
EU Members, March 1999

	Pump price	Taxes and duties		Pre-tax price
	per litre	per litre	% of pump price	per litre
Belgium	£0.39	£0.26	66%	£0.13
Denmark	£0.42	£0.29	68%	£0.13
Germany	£0.38	£0.26	69%	£0.12
Greece	£0.33	£0.22	67%	£0.11
Spain	£0.36	£0.23	63%	£0.14
France	£0.43	£0.33	75%	£0.11
Ireland	£0.44	£0.29	67%	£0.15
Italy	£0.49	£0.35	72%	£0.14
Luxembourg	£0.34	£0.21	62%	£0.13
Netherlands	£0.44	£0.30	66%	£0.15
Austria	£0.41	£0.26	64%	£0.15
Portugal	£0.36	£0.25	68%	£0.11
Finland	£0.42	£0.28	66%	£0.14
Sweden	£0.46	£0.28	62%	£0.18
United Kingdom	£0.68	£0.57	84%	£0.11
EU Average	£0.42	£0.29	69%	£0.12

Note: Prices converted to sterling on basis of exchange rates on 29 March 1999

Source: EU *Weekly oil bulletin*

D. Eurovignette and Tolls

Owners of UK registered HGVs, having paid vehicle excise duty here, do not have to pay vehicle excise duty abroad but they may have to pay road user charges or road tolls.

The eurovignette is an additional road user charge, based on the amount of time that a vehicle uses the infrastructure network. It was introduced for trucks in Germany, Denmark, and the BENELUX countries on 1 January 1995 and involves the display of a vignette to be displayed on all HGVs over 12 tonnes using the road system. Sweden joined in 1997. Germany was the first to initiate the system as a result of concern at the number of trucks using its roads. It applies to all HGVs whether they are registered in one of these countries, in the rest of the EU or outside the EU. The EU legislation sets out an

[28] Table supplied by Paul Bolton, General and Social Statistics Section

annual maximum rate (1250 ECUs, about £840) and does not allow a vehicle to be charged both a distance based tax, such as road tolls or electronic charging and a time based charge such as the eurovignette.[29] France therefore charges road tolls and not the eurovignette, as do Italy, Austria, Spain, Greece and Portugal.

The eurovignette is not the same as the road tax although in Belgium the two are collected together. Belgium judges its own hauliers need the eurovignette all year and charges accordingly. UK hauliers buy the vignette in advance as they go through the port and it costs about £4 a day. You buy what you expect to use as refunds are not available, rather like a parking charge.

The Conservative Party has called on the government to cut the tax on British hauliers and recoup the lost revenue by introducing a scheme similar to the eurovignette.[30] This seems to be named the BRIT disc (British Road Infrastructure Tax) and has received support from the FTA.[31] The government has said it will look at the suggestion as part of its general evaluation of the competitiveness of the industry. Legally the UK could introduce the eurovignette. It would not be affected by the UK's existing bridge tolls and the proposed local congestion charging plans: it is only motorway tolls that are covered by the directive. No vehicle can pay both the eurovignette and tolls but the UK could introduce it in the UK for vehicles over 12 tonnes and motorway tolls could be introduced for other vehicles. An eurovignette must apply to both domestic and international traffic so the UK industry would not benefit unless VED was reduced at the same time.

The scheme, as practised on the continent, is a rather unsophisticated, paper based system. Indeed, it is possible that Germany may leave the group as its research into electronic tolling is quite far advanced and it may prefer to introduce an electronic system. If this happened it is not clear whether the others would continue with their eurovignette as much of the administrative cost is currently borne by Germany.

E. Corporation Tax

Details of the rates of corporation tax in the European Union were given in reply to a PQ on 24 March 1999.[32] The amount paid by any individual will depend on the circumstances of the company: small hauliers are unlikely to make much profit and so not pay much corporation tax. Furthermore comparing corporation tax rates can be misleading without looking at the underlying tax systems and the individual country basis of taxable profit. The calculation of taxable profit earned by a company varies widely in the EU. For example, one could look at the tax treatment of goodwill (the difference between what a purchaser pays for a company and the book value of its assets). This is not deductible in

[29] 93/89/EEC

[30] See for example, *Financial Times* 9 April 1999 "Hauliers set to disrupt cities and ports"

[31] See for example, *Daily Telegraph* 13 April 199 "Foreign lorries may face road charges"

[32] PQ HL Deb 24 March 1999 WA161

the UK, Ireland, France, Portugal and Spain, but can be deducted everywhere else. There is a wide range of other variables affecting taxable profit.[33]

The corporation tax rates, as given in the PQ, are:

Lord McIntosh of Haringey: Rates of central government corporate tax in the European Union.[1,2]

EU member state	*Main Rate %*	*Small Companies[1] Rate %*
Austria	34	–
Belgium	40.17[3]	28.84[4]
Denmark	34	–
Finland	28	–
France	36.66/40[5]	20.9[6]
Germany	31.65/42.2[7]	–
Greece	35/40[8]	–
Ireland	28[9]	25
Italy	37	–
Luxembourg	31.2[10]	20.8[11]
Netherlands	35	–
Portugal	34	20[12]
Spain	35	30
Sweden	28	–
United Kingdom	30[13]	20[14]

Notes: In the notes below the surcharges apply after calculating tax at the rates shown.
[1] January 1999 except for UK.
[2] Some countries, including the United Kingdom, operate tapers that smooth out the transition when moving between different rates. This can give rise to average rates of tax lying between the rates shown in the table.
[3] 39% plus 3 % austerity surcharge. Under certain conditions reduced rates may apply.
[4] 28% plus 3% austerity surcharge.
[5] 33.33% plus surcharges of 10% and 20% respectively, the latter applying to companies with turnover of more than FFSO million.
[6] 19% plus surcharge of 10%.
[7] 30%/40% for distributed/retained profits respectively plus 5.5% solidarity surcharge.
[8] The lower rate applies to companies (other than banks) quoted on the Athens Stock Exchange.
[9] 25% on the first IR£100,000. An effective rate of 10% rate applies to manufacturing and many internationally traded services.
[10] 30% plus 4% unemployment surcharge.
[11] 20% plus 4% unemployment surcharge.
[12] For qualifying small companies. A temporary tax holiday is available to small companies formed from 1 January 1999. " From 1 April 1999.
[13] From 1 April 1999.
[14] From 1 April 2000 there will also be a 10% starting rate.

[33] See *Financial Times* 9 December 1998 "Reforms essential to find true harmony"

F. Labour Costs

[This section is contributed by Robert Twigger, Economic Policy and Statistics Section]

Up-to-date statistics for the road haulage industry are not available, however, information for manual workers in manufacturing industry suggests that hourly labour costs in the UK are below those in most EU countries and that this is partly explained by lower statutory costs.

The following analysis is based on data published by the US Bureau of Labor. The data relate to hourly compensation costs in US dollar terms. Compensation costs include hourly direct pay, employer social insurance expenditures and other labour taxes. A fuller description is given in the technical box on page ??. Data for 1997 are set out in the following table.

Hourly Compensation Costs: 1997

Production workers in manufacturing

Country	Total		Composition				
	US dollars	Index UK =100	Direct pay: For time worked	Direct pay: Other	Direct pay: Total	Social insurance & other taxes	Total
Austria	21.92	142	50.9%	21.6%	72.4%	27.6%	100.0%
Belgium	22.82	148	52.7%	19.0%	71.8%	28.2%	100.0%
Denmark	22.02	142	82.2%	12.9%	95.1%	4.9%	100.0%
Finland	21.44	139	58.1%	19.0%	77.1%	22.9%	100.0%
France	17.97	116	52.6%	16.2%	68.8%	31.2%	100.0%
Germany (West)	28.28	183	54.4%	19.7%	74.0%	26.0%	100.0%
Greece (a)	9.59	68	58.5%	19.3%	77.8%	22.2%	100.0%
Ireland	13.57	88	76.1%	9.5%	85.6%	14.4%	100.0%
Italy	16.74	108	50.7%	17.7%	68.4%	31.6%	100.0%
Luxembourg (a)	22.55	160	70.2%	16.1%	86.3%	13.7%	100.0%
Netherlands	20.61	133	58.0%	19.4%	77.4%	22.6%	100.0%
Portugal	5.29	34	n.a.	n.a.	76.6%	23.4%	100.0%
Spain	12.16	79	n.a.	n.a.	74.4%	25.6%	100.0%
Sweden	22.24	144	59.8%	11.8%	71.7%	28.3%	100.0%
United Kingdom	15.47	100	75.3%	11.9%	87.1%	12.9%	100.0%

Note: (a) Data for 1996.

Source: BLS, *International Comparisons of Hourly Compensation Costs for Production Workers in Manufacturing*, 1975-1997, Supplementary tables

In 1997 a number of EU countries including (West) Germany, Austria, Belgium, Denmark, the Netherlands and Sweden had levels of hourly compensation for production workers in manufacturing costs more than one-third above those in the UK. With the notable exception of Denmark, the UK had the highest proportion of total costs accounted for by direct pay and the lowest proportion relating to social insurance and other labour taxes.

In the short-term the exchange rate can have a significant impact on relative labour costs. However, sterling is currently trading at levels broadly similar to those of 1997. In terms of overall competitiveness, labour costs are not the only consideration. Factors such as productivity are also relevant.

Technical box

Definition of Compensation Costs

Hourly compensation is defined as (1) hourly direct pay and (2) employer social insurance expenditures and other labour taxes. Hourly direct pay includes all payments made directly to the worker, before payroll deductions of any kind, consisting of (a) pay for time worked (basic time and piece rates plus overtime premiums, shift differentials, other premiums and bonuses paid regularly each pay period, and cost-of- living adjustments) and (b) other direct pay (pay for time not worked (vacations, holidays, and other leave, except sick leave), seasonal or irregular bonuses and other special payments, selected social allowances, and the cost of payments in kind). Social insurance expenditures and other labour taxes includes (c) employer expenditures for legally required insurance programmes and contractual and private benefit plans (retirement and disability pensions, health insurance, income guarantee insurance and sick leave, life and accident insurance, occupational injury and illness compensation, unemployment insurance, and family allowances) and, for some countries, (d) other labour taxes (other taxes on payrolls or employment (or reductions to reflect subsidies), even if they do not finance programmes that directly benefit workers, because such taxes are regarded as labour costs). For consistency, compensation is measured on an hours-worked basis for every country.

The BLS definition of hourly compensation costs is not the same as the International Labour Office (ILO) definition of total labour costs. Hourly compensation costs do not include all items of labour costs. The costs of recruitment, employee training, and plant facilities and services - such as cafeterias and medical clinics - are not included because data are not available for most countries. The labour costs not included account for no more than 4 percent of total labour costs in any country for which data are available.

III The Interested Parties

A. The Government

Although this paper concentrates on the government's response to the particular debate about increased taxes on the road haulage industry in comparison with other European countries, some general material is included in the following paragraphs.

1. The cost debate

The costs of the haulage industry were raised at some length during an adjournment debate in the House of Commons in November 1998.[34] When asked about a level playing field, the minister, Ms. Hewitt responded (her references are to the 1998 budget):

> We are conscious of the impact of higher fuel taxation and VED on competitiveness and profitability, but it needs to be put into a wider context. The United Kingdom has lower corporation taxes, lower employment taxes and lower social costs than other European Union countries, especially with my right hon. Friend the Chancellor's recent Budget measures to assist small businesses. The overall tax burden is lower in the United Kingdom than in our major EU competitors and lower than the averages for the EU and the Organisation for Economic Co-operation and Development. [Interruption.]
>
> Not only is the overall burden of taxation lower on British businesses - including the road haulage industry - than on European businesses, but looking at business as a whole, transport is a relatively small part of total business costs. …Tax measures that we have recently introduced, or will introduce, to help road hauliers include the freezing of the standard VED rates for lorries. That means that lorry drivers are paying less VED in real terms than they were in 1990, which partly offsets the impact of higher fuel duty and should help to maintain the competitive position of our road hauliers. A reduction of up to £500 in VED for low emission lorries and buses will be introduced at the end of this year. There is also the freeze in duty on road fuel gases and the widened differential that we will maintain and, I hope, increase, in favour of ultra-low-sulphur diesel.
>
> There were broader measures in the Budget that will benefit business and road hauliers: the 1 per cent cut in the main rate of corporation tax; the 1 per cent cut in the small companies rate of corporation tax, which next April will be down to 20 per cent; the introduction of quarterly payments for large companies, replacing advance corporation tax; the extension of enhanced temporary first year capital allowances; and the introduction of the taper to reduce the capital gains tax on assets held for longer periods, which is equivalent to a higher tax rate of 10 per cent. after 10 years on business assets.

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[34] HC Deb 11 November 1998 cc 342-9

Mr. Paterson: … [The minister] mentioned the environment, but why have not other European countries imposed a fuel escalator if it is such a good idea? They signed up to Kyoto. She talks about the contribution of the industry to the environment, but £30 billion is taken from road users while only £2 billion is spent on roads.

Ms Hewitt: The point of environmental taxation is to internalise the external costs imposed, in this case by road users, in the prices that they are charged, not necessarily to return the product of that revenue directly to them. Several EU member states, including the new German Government, are considering carefully proposals for carbon tax and energy tax. There are proposals at European level for an energy tax, which we will consider carefully.

Hon. Members raised competition from abroad. Despite what has been said, there is little evidence of foreign hauliers undercutting domestic hauliers for business in the United Kingdom. …

The fact is that less than 0.04 per cent UK road miles are done by foreign hauliers. The long-term outlook for the industry in this country suggests that lorry traffic is expected to grow by more than 60 per cent in the next 20 years, an enormous growth in that sector of the economy. That makes it imperative that the Government ensure, by effective use of taxation, that the lorries on the road are the most fuel efficient and environmentally friendly available.

Under EU legislation - I think that the hon. Member for North Shropshire welcomed this - hauliers are free to set up business anywhere in the European Union. That is a commercial decision for the businesses involved. Let me remind him that many other factors are involved besides the prospect of cheaper vehicle licence or fuel tax: the setting up costs; the burden of obtaining an operator's licence; higher drivers' wages; considerably higher social costs; higher corporation tax rates - and so on. Setting up a business on the continent has all those obvious costs. When all taxation is taken into account, the burden on business in the United Kingdom is lower than in other European Union states. Any British haulier who decided to set up in France or Belgium might find that road fuel taxes went down, but would certainly find that his social costs and wages bill went up. It is, therefore, not surprising, when one considers the overall burden on business, that there have also been reports in the trade press of French hauliers registering their businesses in the United Kingdom to take advantage of lower business costs and the opportunities to grow their businesses.

The hon. Member for North Shropshire suggested that environmental taxes are simply an excuse for revenue raising. That is not the case. We are developing environmental taxes in line with the statement of intent on environmental taxation and with a vital principle both of market economics and of environmental concerns: prices should reflect true costs so that the polluter pays..[35] Fuel duty

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[35] HM Treasury press notice 2 July 1997 "Tax measures to help the environment". This is reproduced in the next section

> increases are important to encourage further improvements in fuel efficiency and reductions in carbon dioxide emissions. Our spending is directed towards the people's priorities of education and health, from which everyone benefits, but also to increased spending on rural transport, which, as I hope that he agrees, will be of particular benefit to rural communities.

The Transport Minister, John Reid spoke in a debate on roads on 18 March 1999, after the Budget, and referred to the road haulage industry as follows:[36]

> **Dr. Reid**: …For a fleet of 50 38-tonne trucks, if we include the social costs, national insurance, taxation, corporation tax, employees' costs, fuel and vehicle excise duty, the additional cost in France, as compared with the United Kingdom, is about £425,000 a year; in the Netherlands, about £600,000; and in Belgium, about £800,000.
>
> I take the competitiveness of the road haulage industry extremely seriously. …I understand that it is a fiercely competitive world and that there is overcapacity in the United Kingdom; but let us not exaggerate to the extent of blaming all the problems with competitiveness on the fuel escalator or on VED. We need a balance if we are to do justice to the industry. …
>
> Let us examine some of the Budget measures. We have reduced main corporation tax to 30 per cent and small companies corporation tax to 20 per cent. Moreover, from 1 April 2000, companies with profits of up to £10,000 will pay corporation tax of only 10 per cent. Companies with profits of up to £50,000 will benefit from relief given to ease the transition from the new starting rate to the 20 per cent rate. Employees of haulage businesses will benefit from the new 10p starting rate of income tax from this April and employers will benefit from reduced national insurance contribution levels from 2001.
>
> Those are only the general initiatives; the Budget also contained specific measures for hauliers. We have frozen road duty levels for 98 per cent of all lorries - I thought that the Opposition would applaud that move. The reduction in VED for cleaner lorries has doubled from £500 to £1,000. The duty rates on ultra-low sulphur diesel have been reduced relative to ordinary diesel and the duty rates on road fuel gases have been cut by no less than 29 per cent - one of the biggest ever cuts in duty.
>
> The Opposition's suggestion that the Budget does nothing for haulage firms is a grotesque misrepresentation of the facts. It is all about balance. Vehicles with an 11.5-tonne drive axle weight - to which the Opposition like to refer - cause significant road damage. That is why their road duty rates were set as they were, although we froze 98 per cent of other rates.

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[36] HC Deb 18 March 1999 c 1334

> The Opposition are also suffering from amnesia about the fuel duty escalator. I remind the House that the previous Government introduced the fuel duty escalator in 1993 and committed themselves to maintaining it until 2000. The right hon. Lady [Mrs. Gillian Shephard] accused us of placing a burden on industry of 6 per cent. a year. She seems to have forgotten that 5 per cent was imposed by the Conservatives and only 1 per cent by Labour. We made that imposition in recognition of our need to act if we are to continue to lead the world on climate change.
>
> As for the firms that are moving abroad to avoid the so-called excessive burdens, I gave the comparative figures for the whole cost earlier in the debate. I admit that it is a complex matter: I do not suggest for a minute that it is not possible to engineer a formula that would achieve savings. I want to talk to the industry about that and other matters. However, international haulage firms with 50 38-tonne lorries based in the Netherlands and Belgium - the countries with which we are invited to make a comparison - will face costs additional to the levels that I outlined earlier.

According to a *Sunday Times* article, which quotes these figures used by John Reid, the figures are backed by a report from KPMG.[37] The report was also referred to by the secretary of state, John Prescott on 14 April.[38] The KPMG report was commissioned by the Canadian High Commission and compares the costs of doing business in 64 cities in eight countries. It found that Canada was the lowest cost country overall but it also found that the UK had the lowest labour costs and the UK and Germany had the lowest transportation costs, amongst the countries examined. Germany held the lowest road freight costs while the UK held the advantage in sea freight.[39]

2. Policy documents

The Labour Party made no specific reference to the road haulage industry in its election manifesto. It referred to the need for a sustainable environment which in turn depended on an effective and integrated transport system.[40] It set out its support for small businesses but stressed at all points the importance of protecting the environment.

In his first Budget speech in July 1997, the Chancellor Gordon Brown, set out the Government's priorities in environmental taxation, which included the publication of a statement of 'environmental principles':

> A country equipped for the future should also have a modern tax system based on principle. The tax system sends critical signals about the economic activities that

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37 *Sunday Times* 28 March 1999 "Angry truckers exodus could cost 53,000 jobs"

38 HC Deb 14 April 1999 c 222

39 KPMG press notice 11 March 1999 "UK business costs lowest in Europe, new research finds"; *Comparison of business costs in Canada, Europe and the United States* 1999 Executive summary [full report is not available in the Library]

40 Labour Party election manifesto *New Labour: because Britain deserves better* 1997 p 29

> a society wishes to promote and deter. Today I shall start to put those principles into practice by demonstrating our commitment to the environment. As the statement of environmental principles set out by the Financial Secretary to the Treasury, my hon. Friend the Member for Bristol, South (Dawn Primarolo)--published today--shows, we are determined that our tax system and economic policies as a whole encourage the good and discourage the harmful.[41]

The Government's statement of intent was published in a Budget press notice, and is reproduced below:

> The Government's central economic objectives are the promotion of high and sustainable levels of growth and high levels of employment. By that we mean that growth must be both stable and environmentally sustainable. Quality of growth matters; not just quantity. Delivering sustainable growth is a task that falls across government. It will be a core feature of economic policy under this administration. The Treasury is committed to that goal.
>
> How and what governments tax sends clear signals about the economic activities they believe should be encouraged or discouraged, and the values they wish to entrench in society. Just as work should be encouraged through the tax system, environmental pollution should be discouraged.
>
> To that end, the Government will explore the scope for using the tax system to deliver environmental objectives - as one instrument, in combination with others like regulation and voluntary action. Over time, the Government will aim to reform the tax system to increase incentives to reduce environmental damage. That will shift the burden of tax from "goods" to "bads"; encourage innovation in meeting higher environmental standards; and deliver a more dynamic economy and a cleaner environment, to the benefit of everyone. But environmental taxation must meet the general tests of good taxation. It must be well designed, to meet objectives without undesirable side-effects; it must keep deadweight compliance costs to a minimum; distributional impact must be acceptable; and care must be had to implications for international competitiveness. Where environmental taxes meet these tests, the Government will use them.[42]

One question posed in *A new deal for transport: better for everyone*, the 1998 transport white paper, was how to deliver goods efficiently and with least harm to the environment and health.[43] Its conclusion was that the government would work in partnership with the industry to promote sustainable distribution, by which it meant "improving the efficiency of the distribution market in a way that meets our environmental objectives." The government published its more detailed strategy in March 1999. *Sustainable distribution: a strategy* has a section on "Fair pricing" much of which is reproduced here:[44]

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[41] HC Deb 2 July 1997 c 311

[42] HM Treasury press notice 2 July 1997 "Tax measures to help the environment"

[43] Op cit, *A new deal for transport* paras 3.154-3.177

[44] Op cit, *Sustainable distribution* para 4.15-4.26

4.15 A sustainable market is more than just an open market. In a sustainable market decisions are taken in cognisance of their wider impact, and decision-makers act responsibly with respect to society as a whole, both today and over the longer term. In order for this to happen it is important that the market should properly inform decision-makers as to the wider costs which they are incurring in taking their decisions - and not only those costs which bear directly upon themselves. This issue was explored in the previous Government's transport Green Paper in 1996 and by the European Commission in a Green Paper "Towards Fair and Efficient Pricing in Transport", published in December 1995. The Commission has now published a White Paper, developing this agenda for transport infrastructure charging.

4.16 A substantial element of distribution costs is typically "internal" to the buying transaction and therefore taken into account as a matter of course through the operation of the market. Thus the purchaser or operator of road haulage services must consider all the labour, fuel, vehicle depreciation and maintenance costs (including taxes) which make up to the bill for getting goods from A to B.

4.17 However in reality the costs do not end there. In the process of getting from A to B a vehicle consumes road space, which itself has a cost. It contributes to wear and tear which will eventually necessitate expenditure on maintenance of road surfaces and structures, and to congestion incurred by other road users. Collectively road traffic is a substantial cause of deaths and injuries, which impose heavy costs on society at large, through the NHS and in terms of lost output, grief and suffering. Some of these costs do reflect back on the operator or purchaser of transport services in due course, for example through insurance premiums and through taxation to fund public expenditure on road building and maintenance. But they are not reflected completely, nor are they always directly apparent.

4.18 Then there are still wider "external" costs. These include the impact of vehicle emissions on local air quality, public health and climate change. Nearly everyone, every day, is affected in some way by noise and congestion on our crowded roads and city streets, including car, van and lorry drivers themselves. Typically these costs are not directly apparent to the transport purchaser or operator, at least in the short term.

4.19 The Government can promote fair and transparent pricing through taxation. This Government has adopted a strategy of annual increases in fuel duty of at least 6% on average above inflation, and is committed to move towards a fairer treatment of petrol and diesel, when calculated on an energy or carbon-content basis. These are significant steps towards reflecting the wider costs of road transport in the prices that users pay.

4.20 The Government recognises the haulage industry's concern that the fuel duty escalator makes fuel in the UK more expensive than in other EU countries. However, the fuel duty escalator is the best way known to encourage fuel efficiency, for which there remains plenty of scope. It is also only one factor in haulage costs, albeit an important one; UK hauliers do benefit from more favourable company taxation and social costs than in many other EU countries.

4.21 The Government can also offer financial incentives. To reflect concerns over air quality, the 1998 Budget increased the differential between ordinary diesel and ultra-low sulphur diesel to 2 pence per litre, and the Government announced a commitment to increase this again, to 3 pence per litre, at the next Budget. The Government has also introduced a VED concession, worth up to £500, for HGVs and buses meeting very stringent emission standards.

4.22 The White Paper proposals in respect of road user charging provide another mechanism for adjusting prices, giving local authorities new opportunities to manage demand for road space and the wider impacts of traffic congestion.

4.23 However, while it is easy to say that pricing should be "fair" in the widest sense, it is more difficult to pin down what "fair" really means. We know, for example, what the total cost of building and maintaining roads is, but it is not a simple matter to attribute elements of that cost to broad categories of vehicles, still less to individual vehicles. Quantification of some of the wider "externalities" (such as the costs of noise or pollution) is yet more difficult. Different approaches to estimation (e.g. "willingness to pay" vs. "mitigation cost") can produce substantially different figures.

4.24 Nevertheless, progress can be made towards taking proper account of these costs through the tax system. As part of the last Budget, the Government announced a wide-ranging review of the system of setting Vehicle Excise Duty (VED) rates for lorries, to reflect the environmental damage which they cause. To assist with this review, the Government has commissioned further research, with the aim of developing cost estimates which command greater confidence both in the industry and in the wider community. Better information should help to promote informed policy development at EU, as well as national, level.

4.25 Another important mechanism for promoting fair markets is regulation, which directly 'internalises' external costs by requiring industry to meet particular standards. This Government supports the European Commission's Auto-Oils programme which seeks to bring about improvements in air quality through progressive reductions in vehicle emissions and improvements in fuel quality. Regulation has also played a strong part in improving the safety of vehicles through design, through driving standards requirements and through the requirements laid down for vehicle operation.

4.26 A third mechanism is partnership, in which industry meets a particular standard or changes behaviour voluntarily so that both industry and society can benefit. Chapter 6 of this document sets out a range of proposals for developing more effective working partnerships between industry and Government at local, regional and national levels.

B. The Road Haulage Organisations

The Road Haulage Association and the Freight Transport Association represent the interests of over 20,000 businesses and their members operate over 250,000 vehicles, nearly two-thirds of the total number of heavy goods vehicles registered in the UK. Prior to the 1999 Budget they issued a joint submission to the Chancellor.[45] They argue that the government's present policies are not only affecting vehicle operators but also pose a threat to the UK economy.

1. Changes to policy

The industry argued for changes in policies on two key issues, fuel duty and VED, in their joint submission to the Chancellor of the Exchequer prior to the 1999 Budget:

Fuel duty

About fuel prices, it said:

> Fuel costs represent one of the biggest single cost items for goods vehicles, often amounting to as much as 35 per cent of total business costs. Increases in fuel duty are therefore of great concern as this affects the cost of one of the primary inputs into the operation of goods vehicles.
>
> As a consequence of the Government's stated long term fuel duty strategy, the UK has by far the highest rate of diesel duty in the EU to the extent of it being more than double the EU average. Until recently, the difference between UK fuel duty rates and continental rates only presented a significant problem for those hauliers operating internationally on a regular basis since they were competing for those contracts with hauliers based outside the UK. In an attempt to minimise the disadvantage they face, hauliers involved in such contracts have adapted their business practices and now purchase nearly all of their fuel abroad. Whilst this helps the haulier by improving his competitive position, it does have obvious adverse consequences for the UK Exchequer in terms of fuel duty lost. This problem has, of course, been compounded by the hardening of Sterling against the principal continental currencies in recent years.
>
> The difference in fuel duty rates became a serious threat to all LTK goods vehicle operators from July 1998 following the removal of all EU cabotage restrictions. This gave continental based hauliers the right to seek domestic business in the UK, competing against LTK hauliers. The much lower price of fuel available to continental-based hauliers has given them a competitive edge and the Government's policy of escalating fuel prices in the UK will simply widen this advantage.

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45 FTA/RHA joint submission to the Chancellor of the Exchequer *Budget 1999*

> Historically, only a relatively small proportion of goods is carried on domestic journeys by vehicles registered outside the LTK. It is this fact that has led Government to the mistaken belief that the threat posed by the removal of cabotage restrictions and higher fuel duties is being over estimated. However, this assumption fails to take account both of the amount of cabotage work that was carried out in the LTK prior to their abolition without permits, and also of the effect of an ever-widening fuel price differential. As fuel on the continent becomes cheaper (relative to the LTK) domestic operations within the LTK will become increasingly attractive since continental based hauliers will find it easier to offer lower rates compared to LTK hauliers.
>
> The threat to domestic hauliers from continental-based operators using cheaper fuel is real. A typical tractor unit can legally carry enough fuel to travel at least 1,000 miles. On average that would represent close to a week's normal work for a LTK-based unit.

The industry argue that relief be given immediately by a freeze on diesel duty, accompanied by variable VED on diesel cars, and for the introduction of an "Essential User Rebate" for lorries over 3.5 tonnes. This would allow essential users to claim a rebate on fuel used for business purposes equivalent to the difference between the UK rate and the EU average. Apparently the French introduced a similar scheme in January 1999 for hauliers purchasing their fuel in France. The scheme is subject to a maximum of 40,000 litres and applies to vehicles over 12 tonnes.

Vehicle Excise Duty

The two organisations fear that the review currently looking at the basis of VED will include the external costs of goods vehicle operation within VED rates. It considers that no other sector of business is taxed on this basis and no other member state attempts to recover these costs from its goods vehicle operators. It also argues that the very high rate of VED for the 40 tonne 5 axle vehicle creates a significant cost disadvantage compared to continental operators

2. Effects of the policies

The RHA commissioned a report from the Centre for Economics and Business Research Ltd (CEBR) about the effects on the UK industry of the policies. According to the extract of the report quoted in the joint submission, as a result of the government's fuel policies, the UK would suffer job losses of 53,000 and a reduction of £2.1 billion in GDP (2%).[46]

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[46] RHA press notice 1 July 1998 "Hauliers fear over EU fuel threat"; Joint Budget submission para 3.4

Since the Budget there has been extensive press coverage of their concerns with a number of reports that companies may choose to register abroad.[47] The FTA/RHA explain:

> This progressively higher tax base is seriously eroding profit margins in the haulage sector and as a result is forcing many operators to consider the merits of registering their companies and fleets outside the UK ("flagging out"). This will allow them to benefit from the much lower rates of fuel duty, VED and other taxes, while continuing to employ UK drivers and conduct business in the LTK. (The UK merchant fleet underwent a similar irreversible flight from uncompetitive UK taxes and trading conditions during the 1980s).
>
> The economics of "flagging out" are such that large numbers of operators are likely to take this option and some have already done so. Further increases in UK taxation will only increase its attractiveness, particularly for those with contracts in the South and East of England. A significant migration of UK haulage businesses to the Continent would result in huge losses to Government of tax revenues from fuel duty, VED, O-licence fees and VAT but ironically, no reduction in emissions from vehicles operating on LTK roads. This action would be hastened were major LTK transport users to begin switching haulage contracts from LTK operators to continental-based operators due to the lower rates being offered. The likelihood of this happening will increase with further widening of the differences between LTK and continental taxation rates.

3. A more efficient industry

There are improvements or changes which could be made to the industry which would improve its efficiency. The *Financial Times* summarised them as:[48]

- Designing more fuel-efficient engines and monitoring fuel consumption more closely. Modern engines can respond to fluctuating temperatures and operating conditions to ensure fuel is used sparingly. One company cut fuel consumption by 7 per cent within 12 months of installing such equipment.

- The design of trucks and trailers. This can increase the volume or weight of goods carried and reduce wind resistance and fuel consumption. Wincanton introduced double-deck trailers with the lower deck carrying Marmite and Bovril to customers and the upper deck empty yeast containers for return to local breweries. This did away with separate journeys. Aerodynamic styling of vehicles can cut fuel consumption by 16 per cent.

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[47] See, for example, *Times* 17 March 1999 "Britain's defiant truckers haul up their flag of convenience"; *Financial Times* 17 March 1999 "March hard-pressed hauliers may seek a lighter load across the Channel"

[48] *Financial Times* 22 March 1999 "Signposts on the route to cutting haulage costs"

- Route-planning technology. Computerized methods of route planning can reduce journey requirements. Satellite tracking systems, on-board computers and mobile telephones mean trucks can be re-routed at short notice. If hauliers can persuade customers to share vehicles with other companies, shipments could be combined. Empty running accounts for just under 30 per cent of all truck journeys but this can be reduced by combining deliveries with collections. Safeway developed a Pounds 10m business using its empty returning trucks to pick up consignments for other shippers.

- Using cheaper, environmentally acceptable fuels. A 29 per cent cut in the duty on road fuel gases in the Budget means compressed natural gas carries 35.78p less duty per litre than ultra-low-sulphur diesel. Converting truck engines is expensive and the number of gas outlets is limited but Mobil says hauliers now have a more attractive alternative to diesel.

- Bigger trucks. Increasing the size of loads that can be carried reduces fuel consumption. The haulage industry wants 44-tonne vehicles to be allowed - at present they are restricted to journeys to rail terminals - but there is strong opposition from environmental lobbyists and residents groups.

- Shift to alternative modes. The government is keen to persuade hauliers to move more by rail and by coastal shipping. Rail accounts for just 6 per cent of all freight, but rail freight companies say they can treble shipments over the next few years. Eddie Stobart, Exel and Sainsbury are increasing use of rail but memories of the poor service provided by British Rail still deter many.

Lawrence Christensen, the FTA's president is quoted as saying that progress can be made in all of these areas, although sometimes conflicting environmental objectives add to the industry's costs. Tough emission controls reduce pollution but they also reduce engine fuel efficiency. Emission standards are due to step up a further notch when what are known as Euro 3 engines become a requirement in 2000. Controls on night-time deliveries in town centres are demanded by residents and councils but mean roads cannot be used when they are least congested. Safeway has to operate an additional 100 tractor units and 200 trailers because of night-time delivery restrictions.

C. The Environmental Organisations

Although the road haulage companies have had most of the publicity recently, environmental groups, such as Friends of the Earth, are firmly behind the government's policy. Duty increases help cut pollution levels and encourage hauliers to use rail freight.

IV European Union

A. The 1993 Directive

The European Commission published a consultation document in December 1986 on the *Elimination of distortions of competition of a fiscal nature in the transport of goods by road: study of vehicle taxes, fuel taxes and road tolls.*[49] This was followed by a draft directive in 1987 and eventually minimum rates of vehicle tax, based on gross vehicle weight and axle configuration, and harmonised rules for charging motorway tolls or user charges, were established under an EC directive agreed in October 1993.[50] This prescribed minimum rates of vehicle tax for heavy goods vehicles and the conditions under which tolls or charges may be imposed on such vehicles for the use of motorways. The proposed minimum rates of vehicle tax were introduced on 1 January 1995 and were to remain until the end of 1997, when they were to be subject to review. France, Greece, Italy, Portugal and Spain were allowed to apply rates down to half as much as the minima until the end of 1997. (It is assumed that these states have now raised their tax rates). The second part of the directive allowed member states to impose tolls or user charges up to a maximum annual amount of 1,250 ECU on motorways, bridges, tunnels and mountain passes, and other similar roads on a non-discriminatory basis.

However, in July 1995 the European Court of Justice ruled that the directive was invalid, because the Council had not followed the procedure for Parliamentary consultation strictly enough. Though this ruling had no practical consequences - the directive remains in force until a replacement is adopted - it meant the EC had to look afresh at the issue of pricing in road haulage.

A member state may charge vehicles registered in its own country for the use of its whole road network. A late addition to the directive allowed two or more member states to co-operate in introducing a common system of user charges, so that payment of a single charge gives access to the network of each participating state. Until 1997 they could charge reduced rates to vehicles registered in certain disadvantaged states. In an agreement separate from but related to the directive, Germany agreed with Belgium, Denmark, Luxembourg and the Netherlands to institute a common system of user charges for their five countries from January 1995. This involved the display of the vignette described in Part II.D to be displayed on all heavy goods vehicles of using their road system. These five agreed to charge half the normal rates for two years to vehicles registered in Ireland and Portugal and for three years to vehicles registered in Greece. Although these agreements have expired, they seem to be continuing on an informal basis.

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[49] Doc 11530/86

[50] 93/89/EEC

B. Draft directive on the charging of certain goods vehicles for the use of certain infrastructures

A draft text to replace Directive 93/89/EEC was first produced by the Commission in the early summer 1996, but the reaction to the proposals was particularly hostile. The final text was toned down but even this was more complex than the directive it was to replace and inevitably more controversial.[51] It covered tax policy as well as road charges which immediately gave rise to discussions of subsidiarity and it also included a formula for an environmental charge, which was questioned. At the time the UK government raised formidable objections but many of these were met by a compromise text initiated by the Dutch presidency at the beginning of 1997.

The subject became politically complicated by the linking of the proposed directive on HGV taxation and road user charges to the question of charges for lorries transiting the Alpine routes, especially the Brenner Pass. Austria imposed a charge of Ecu80 as a result of the diverted traffic caused by the Swiss ban on lorries over 28 tonnes. This was considered excessive by the Commission and other member states. Austria refused in December 1997 to agree to the directive without an Alpine clause allowing it to maintain high tolls for the use of the Brenner pass. Agreement was eventually reached on 1 December 1998 when Switzerland agreed to gradually lift its ban on lorries over 28 tonnes.

A draft directive on road user charges was agreed by EU transport ministers on the same day and adopted by the Council of Ministers on 18 January 1999.[52] It still has to be considered by the European Parliament. It could come into force on 1 July 2000. It sets a minimum level of road user charges computed in the light of vehicle environmental performances. Differential prices will be charged according to environmental performance. The main impact for the UK industry would be an increase in the eurovignette daily rate from 6 ECUs to 8 ECUs. This is the first increase since 1995.

C. Towards Fair and Efficient Pricing in Transport

The Commission's green paper, *Towards Fair and Efficient Pricing in Transport*, has already been mentioned as one of the few sources of comparative material on road taxes in the member states of the European Union.[53] The authors found that the relation between total taxes paid and damage caused to the infrastructure was generally poor, as there was no link to mileage in the annual vehicle tax systems. It also found that although minimum levels of annual circulation taxes and maximum levels for road user charges are laid down for

[51] EC draft 11642/96; Com (96) 331 final, 14 November 1996
[52] 10436/98; COM (1998) 427 final
[53] Op cit, COM (95) 691 final 20.12.95

commercial vehicles in community law, the actual rates applied still differed significantly. This was also true of fuel excise duties.

The report concluded that efficient charging implies that charges should be linked as closely as possible to costs. As infrastructure and congestion costs vary significantly, an efficient system will have to be able to differentiate accurately. The objective is not to equalise charges across Europe since infrastructure costs for the same type of road vary according to local/national circumstances, but to make infrastructure charges more transparent and fairer by basing them on the same principles and methods. This is particularly important in the case of heavy goods vehicles where a fair, non-discriminatory charging system is seen as essential for the elimination of the distortion of competition among EU hauliers. It concluded that a kilometre tax would be an option for the medium term. This can accurately take account of vehicle characteristics which determine noise, emissions and road damage.

The Commission argued that the differences shown pointed to a potential distortion of competition between hauliers of different nationalities. Hauliers operating the same vehicles and carrying identical consignments were charged differently on the basis of their nationality. This, in turn, constituted an obstacle to the efficient functioning of the internal market. The report suggested that more harmonisation of minimum levels was needed to create a level playing field for hauliers of different nationalities. The Transport Commissioner, Neil Kinnock, also proposed that the system for standard charges on road freight hauliers, known as Eurovignettes, should be replaced with variable charges related to the age of vehicles, to relate the size of charge to the damage that a vehicle causes to the road infrastructure.

The then UK Government's response to the Green Paper was given in a memorandum submitted in March 1996:[54]

> 9. The UK Government welcomes the broad principles outlined in the Commission's Green Paper of increasing the role of pricing and the use of economic instruments. In the UK, we are already engaged in the process of putting increasing emphasis on the need for pricing structures in transport to reflect full costs, including environmental ones, and in seeking to establish appropriate monetary values.
>
> 10. The specific measures implied by the paper need careful consideration from the point of view of costs and benefits, of practicality and of subsidiarity. The last is particularly important given the emphasis on fiscal measures. Furthermore, many of the impacts of transport are essentially local which suggests that they would be better dealt with at Member State level. In addition, the UK Government would have difficulty if this philosophy were applied to

[54] Department of Transport, *Explanatory Memorandum on Commission Green Paper on Policy Options for Internalising the External Costs of Transport*, 10 March 1996

transport users but not other major producers of externalities. The possible implications for those living in rural areas, whose transport choices are often limited, must also be borne in mind.

11. We agree with the theory of internalising external costs. The challenge lies in translating this into practice, a key aspect of which is determining the values of environmental externalities. These values are more uncertain than the Commission paper implies. The paper might usefully, therefore, have put more emphasis on the uncertainties in some of the valuations. An associated major issue is how then to translate costs into pricing particularly if pricing is to vary by time and place.

12. Another, perhaps more basic, aspect is determining which costs are actually external and which are not. For example, the vast majority of congestion costs and certain accident costs are borne internally within the road transport sector. Another basic aspect is that the paper does not make a clear distinction between economic efficiency and equity in distribution between different groups of people.

D. Fair Payment for Infrastructure Use

On the 22 July 1998 the Commission brought forward a new white paper (it did not include legislative proposals) on transport infrastructure charging, *Fair payment for infrastructure use: a phased approach to a common transport infrastructure charging framework in the EU*, to try to remedy the existing diversity in charging regimes between member states and between modes.[55] The aim is to replace a patchwork of charging arrangements with a harmonised "user pays" approach. Charges for using roads, railways, port and air traffic services would be closely aligned to costs including those incurred through accidents, congestion and pollution. It sets out a package of complementary measures in four areas: charges for road use, improved rail services through development of rail structure, development of combined transport and continued improvements in technical standards for lorries.

The main aim of the proposals is to eliminate distortions of competition in transporting goods across Europe. But the paper also claims that the charging framework would enhance the sustainability of the transport system and help ensure sufficient revenue is available to finance new infrastructure projects. Currently, there is a great diversity of infrastructure charging systems and tax structures, between modes and member states. The paper argues that the true costs of congestion, pollution and other external impacts associated with transport, are not adequately reflected in market prices. This is leading to an inefficient level of demand for some modes, distortions in competition (often based on the nationality of the transport provider) and frequently does not allow infrastructure managers to recoup their costs of providing infrastructure.

The Paper proposes a framework of infrastructure charges based on the 'user pays' principle, including a charge for any 'external costs' the user imposes (e.g. on the environment, for accidents, congestion etc), with charges based on marginal costs paid at, or as close as possible, to the point of use. The charging framework is intended to promote sustainable development, providing business with an incentive to reduce the external costs it imposes (e.g. by changing to less polluting vehicles, or switching to other more sustainable transport modes).

The paper notes that changes to charges may not be automatically reflected in final transport prices, as operators may adjust their operations to lower their costs. It also indicates that member states could continue to support public services or services in the general interest through subsidies to offset effects on prices paid by consumers. Additionally, it suggests that the introduction of new transport charges might be accompanied by amendments to existing transport charges and taxes.

The proposed charging framework is supplemented by proposals for efficient infrastructure investment decisions. A comprehensive cost benefit analysis would be required for all new schemes to ensure that benefits outweigh costs. The paper notes that with charges set at marginal social costs new investment schemes may not recover their total costs and that, with increased emphasis on public-private partnerships in the provision of new infrastructure, this may prevent worthwhile projects going ahead. The paper therefore suggests that additional charges - structured to minimise impacts on transport volumes and competition - may need to be imposed to recoup the investment. However, these supplementary charges would be discontinued after the investment costs and the appropriate return on capital had been achieved.

Member states are asked to agree to the principles of the framework. This would set limits within which a Member State could set the charges for each mode and section of infrastructure. It would also be up to Member States to decide how to use the revenues thus generated – e.g. to allocate funds to the infrastructure operators, or to general funds designated for infrastructure. The assumption in the paper is that revenue related to infrastructure costs, including any congestion element of charge, would be retained by the infrastructure manager to fund existing transport provisions and new infrastructure projects.

The paper envisages that the harmonised framework for infrastructure charging would be gradually introduced in three phases. The first phase (1998 to the end of 2000) would seek agreement on methodologies for measuring marginal costs, including external costs, and promoting the idea of charging at point of use. The Commission would be assisted by a committee of government experts who would in turn be supported by independent experts and other stakeholders (transport operators, users, industry, consumers, transport workers and other interested parties). During this phase, the Commission also anticipates the adoption of its 1998 proposal for railway infrastructure charging; the implementation

[55] 10778/98; COM (98) 466 final

of its proposal for a Council directive on airport charges; and the development of a framework for port charges.

The paper suggests that the second phase (2001-2004) would see a greater harmonisation and adaptation of charging systems, especially for heavy goods vehicles and rail transport where a kilometre based charging system, differentiated on the basis of vehicle and geographical characteristics, would be instituted, and in the ports sector where a charging framework would be introduced. The third phase (post-2004) would draw lessons from experiences during the first two phases and would see further implementation of harmonised charging based on marginal social costs and mandatory use in some commercial transport modes.

The paper then goes on to indicate how the framework would apply to each mode. For road transport, the Commission proposes the phased introduction of distance related charges which include external costs. At the same time member states would be encouraged to introduce urban road pricing schemes which were interoperable with these charges.

The government's view was given in the Explanatory Memorandum of 5 October 1998:[56]

> While recognising that the broad thrust of the proposals is consistent with the proposals in the Government's White Paper – *A New Deal for Transport. Better for Everyone*, they raise a number of substantive issues for the UK including the extent to which such community wide guidelines are necessary. Other significant issues include:
>
> - *Taxation policy.* The implications here are not entirely clear, but it is likely that subsidiarity issues would arise since the Commission appears to be intervening in domestic taxation policy. The proposals advocate a fundamental change to distance based taxation. The proposal for Member States to use the revenues generated from 'efficient' prices to allocate funds to infrastructure operators or to general funds designated for infrastructure, go considerably further than the limited hypothecation of local road user charges and parking levies set out in the Government's Transport White Paper. There is some implication that under these proposals individual Member States would in some circumstances be required to reduce transport taxes if direct charges were increased so that the efficient marginal social cost-based prices were not exceeded.
>
> - *Interface with commercial provision of infrastructure.* The proposals do not adequately address the issues of cost recovery and subsidy implications where marginal cost based prices fail to recover the individual infrastructure manager's total costs of providing infrastructure for commercial users. This is likely to be a particular issue for rail infrastructure provision, and in

[56] DETR Explanatory memorandum 5 October 1998

particular Railtrack. There is also the more practical issue of whether marginal cost based prices, which in theory should allow for a rate of return on marginal capital employed, can ever be calculated sufficiently accurately to provide real incentives for infrastructure providers to attract marginal business.

- *Investment appraisal* The emphasis placed on more formal monetised cost benefit analysis as the arbiter of infrastructure investment decisions contrasts with the shift to broader systems of appraisal in the UK announced in the Transport White Paper. While the EU approach is predicated on desirable - but unrealistically rapid - progress with the monetary valuation of environmental impacts, it seems unlikely that the EU proposal would adequately pick up broader policy issues, e.g. of equity and sustainability, which need to be taken into account.

The paper sets out the Commission's aspirations in relation to infrastructure charging. But it is questionable whether all of its proposals are realistic. For example, the timetable for the phased introduction of the proposals seems very optimistic, particularly the likely speed of progress on the technical issues of quantification of the internal and external marginal costs of infrastructure use.

V Statistics

[This section is contributed by Paul Bolton, Social and General Statistics Section]

A. Domestic Freight and Traffic

1. Recent trends

Table 1 shows the growth of road freight since 1974. Road freight traffic increased by 72% between 1974 and 1997, more of this rise was due to the distance the freight was carried rather than the actual weight. Since 1980 the road freight traffic has grown by 67%, this is more than GDP (47%), manufacturing output (26%) and construction output (42%).[57]

Table 1

HGV Road Freight, 1974 to 1997

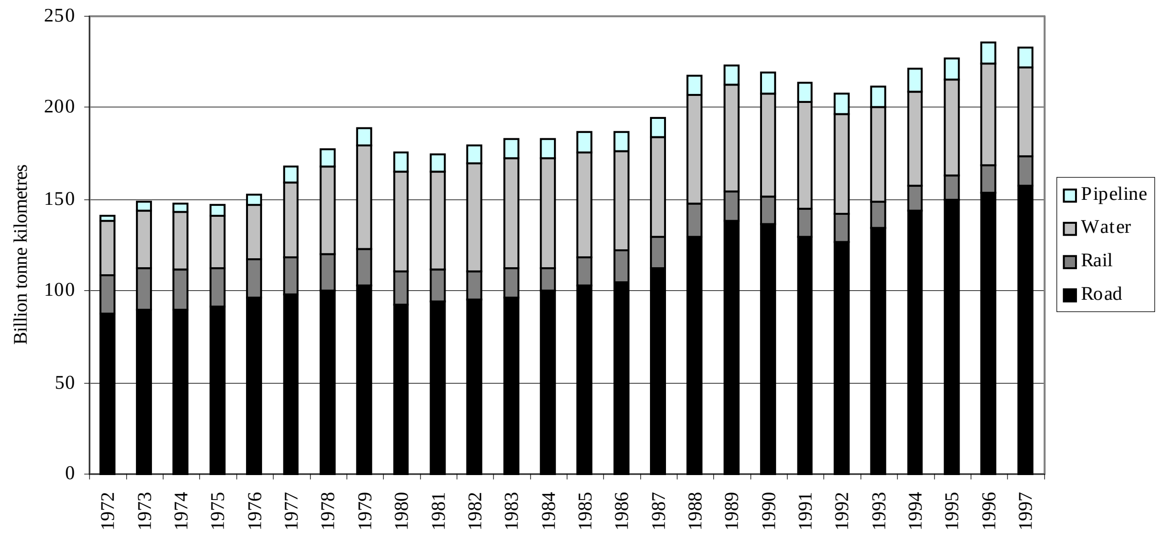
Great Britain

	Road tonnes lifted (million)	Average length of haul (kms)	Road tonne kms (billion)
1974	1,451	60.0	87.1
1975	1,439	61.8	89.0
1976	1,434	64.8	92.9
1977	1,353	70.6	95.5
1978	1,420	67.9	96.4
1979	1,416	70.1	99.3
1980	1,317	68.1	89.7
1981	1,225	73.6	90.2
1982	1,310	69.5	91.1
1983	1,280	72.1	92.3
1984	1,319	73.2	96.6
1985	1,367	72.5	99.1
1986	1,386	72.9	101.1
1987	1,450	74.9	108.6
1988	1,653	75.5	124.8
1989	1,704	77.5	132.1
1990	1,645	79.4	130.6
1991	1,505	82.8	124.6
1992	1,463	82.9	121.3
1993	1,523	84.4	128.6
1994	1,597	86.3	137.8
1995	1,609	89.3	143.7
1996	1,628	90.2	146.8
1997	1,643	91.0	149.6

Source: DETR, Transport of Goods by Road in Great Britain 1997

Trends in goods moved by mode are shown in Figure 1. Road freight has accounted for over 50% of all goods moved for all the years shown. The only significant fall in this proportion was in the late 1970s when there were large increases in goods moved by water.

Figure 1 **Domestic freight transport: Goods moved by mode, 1972 to 1997**



2. Traffic Forecasts

The latest road traffic forecasts estimate that articulated vehicle traffic will double between 1996 and 2026. These forecasts take into account the expected impact of 6% annual real increases in fuel duty to 2002.[58] These rates of increase are the highest of any vehicle type, but somewhat less than that experienced over the last decade.[59]

B. International Road Haulage

UK hauliers export 7½ million tonnes annually and import 8 million[60]. On major bilateral routes within the EU, UK hauliers have market shares of 55% of UK-France goods traffic, 72% of UK-Belgium traffic and 64% of UK-Spain traffic[61]. Over 90% of all

57 DETR *Transport of goods by road in Great Britain 1997*
58 HC Deb 15 April 1999 c299w
59 DETR *National road traffic forecasts (Great Britain) 1997*
60 DETR *Transport statistics Great Britain 1998ibid.*
61 *ibid.*

international road haulage by UK registered vehicles is with the EU. Around 60% of all goods carried overseas go to Germany, France and Italy.[62]

Table 2 looks at the goods moved by the road freight industry in each EU country. There was considerable variation in the proportion of goods moved by road freight, from less than 40% in Luxembourg and The Netherlands to 97% in Greece. In the UK in 1996 just under two thirds of all goods were moved by road freight. This ranked 9th out of all member countries.

Table 2

Goods moved by domestic road freight, EU countries, 1996

	Billion tonne-kilometres	Percentage of all freight transport
Austria[(a)]	15.7	41%
Belgium[(a)]	42.6	75%
Denmark	9.4	66%
Finland	22.1	64%
France	158.2	67%
Germany	203.8	59%
Greece	12.8	97%
Ireland[(a)]	5.4	90%
Italy	197.6	84%
Luxembourg	0.6	38%
Netherlands	27.6	38%
Portugal[(a)]	11.1	83%
Spain[(a)]	183.2	92%
Sweden	31.2	63%
United Kingdom	150.2	64%

(a) 1995 data

Sources: *Trends in the transport sector 1970-1996, ECMT*
Transport statistics Great Britain 1998, DETR

Table 3 illustrates trends in international road freight traffic. Information is only collected on outward journeys, but this can also be seen as a proxy for goods vehicles entering the UK. The number of UK registered vehicles travelling to Europe is now three times higher than it was in 1982. There has been an even larger increase in foreign registered vehicles leaving Great Britain over the period. The most recent two years have seen travel by UK vehicles remain fairly static while there has been a 43% increase in traffic from vehicles registered elsewhere.

62 *ibid.*

Table 3

Powered road goods vehicles travelling from Great Britain to mainland Europe, by country of registration

Thousands

	UK	Foreign	Unknown	Total
1982	181.2	166.4	4.9	352.4
1987	236.8	305.7	0.4	542.9
1988	255.0	342.6	0.1	597.7
1989	295.3	392.9	1.9	690.1
1990	339.0	382.9	1.7	723.7
1991	360.2	362.9	2.4	725.5
1992	373.7	394.1	2.1	769.8
1993	398.0	392.4	5.8	796.2
1994	453.1	439.3	4.0	896.5
1995	486.0	461.2	3.0	950.2
1996	531.1	484.4	2.2	1,017.7
1997	543.2	597.6	5.7	1,146.4
Four quarters ending Q3 1998	544.1	690.6	4.2	1,239.0

Source: Road Goods vehicles travelling to mainland Europe, 3rd quarter 1998, DETR

VI Further Reading

DETR *Focus on freight* August 1998
DETR *A new deal for transport: better for everyone* July 1998 Cm 3950
Transport Retort July 1998 "Lorries 2000"
Debate on road haulage (taxation) HC Deb 11 November 1998 cc 342-9
Environment, Transport and Regional Affairs Committee *Integrated transport white paper*. Minutes of evidence: FTA, 9 December 1998 HC 32-I
Transport Law and Policy December/January 1999 "Fuel escalator"
DETR *Sustainable distribution: a strategy* March 1999
FTA/RHA joint Budget submission 1999
Debate on roads HC Deb 18 March 1999 c 1334