



# FACT SHEET

## Vehicle and fuel taxes plus the removal of car-oriented subsidies

### Key point

- *By internalizing the external costs of purchasing and using private cars, such as congestion and degraded air quality, the overall demand for private cars can be discouraged.*

### Vehicle and fuel taxes explained

Historically, vehicles and fuels have been favoured in financial terms through subsidies and tax breaks, thereby reducing incentives to move towards eco-efficient transport patterns. It is imperative that such financial preferences be removed and that vehicles and fuels are priced in ways that reflect their costs to society and the environment.

### How it works

Taxes on or subsidies for vehicles and fuels are often applied at the national level and are often designed to promote (either intentionally or otherwise) the use of private cars. This trend can be reversed as follows:

Fuel subsidies, which are commonly applied in countries in the Asia-Pacific region, should be removed and instead fuels should be taxed.

The sale and ownership of vehicles should be taxed (such as purchase tax and annual registration tax) and subsidies removed. Value-added taxes (VAT) vary according to the specification of cars and can be regarded as a purchase tax. Many European countries have a special car purchase tax in addition to VAT.

Although the tax on fuel has more direct impacts on the use of vehicle, vehicle-related taxes affect the vehicle choice consumers make when buying (such as fuel efficiency technology and size of engine). Following practice in such countries as the France, Germany, Japan, Spain and the United Kingdom, the tax on vehicles could be made to reflect their environmental performance so that those cars with less fuel consumption would be made cheaper compared with those that are fuel inefficient.

### Strengths in taxing vehicle and fuel and removing subsidies

- Taxes on fuels and vehicles are relatively easier to administer and enforce compared with more localized charges, such as for parking and congestion.
- Transaction costs (the costs associated with their collection) are relatively low.
- These taxes have the ability to raise a significant amount of revenue, which could be invested in public transport improvements.

### Challenges to removing subsidies and raising taxes on vehicles and fuel

- Opposition from industry, particularly the motoring lobby.
- Opposition from consumers, who perceive an increase in the cost of transport.

## Implementing strategies

**Remove subsidies gradually** to mitigate any large price changes within a short period. Targeted subsidies (in the form of cash pay-outs) can be provided to the most vulnerable members of society who may be affected by a rise in the fuel price.

**Use the revenue from the higher level of tax to finance alternative, eco-efficient transport**, such as the construction of public or non-motorized transport infrastructure and the operation of public transport.

**Link the level of vehicle tax to the environmental performance of a vehicle** so that higher-polluting vehicles will be taxed at a higher rate.

## Examples

**Indonesia:** Efforts have been made to reduce the level of fuel subsidies, coupled with measures to reduce public opposition, including the cash transfer to the urban poor.

**Ghana and other African countries:** Revenues from fuel taxes are being used to maintain road infrastructure in a consistent manner.

## Further reading

*International Fuel Prices*, by GIZ (Eschborn, Germany, 2010). Available from [www.gtz.de/en/themen/29957.htm](http://www.gtz.de/en/themen/29957.htm).

“Module 2b: Mobility Management”, by Todd Litman, *Sustainable Transport: A Sourcebook for Policy-Makers in Developing Cities* (Eschborn, Germany, GTZ (GIZ), 2003). Available from [www.vtqi.org/gtz\\_module.pdf](http://www.vtqi.org/gtz_module.pdf)

*The Effects of Fossil-Fuel Subsidy Reform: A Review of Modelling and Empirical Studies*, by Jennifer Ellis (Geneva, International Institute for Sustainable Development, 2010). Available from [www.globalsubsidies.org/files/assets/effects\\_ffs.pdf](http://www.globalsubsidies.org/files/assets/effects_ffs.pdf)