

Fifty-Fifth Report of Session 2019–21

HM Treasury and HM Revenue and Customs

Environmental Tax Measures

Introduction from the Committee

The government has ambitious environmental objectives. The UK is legally committed to bringing all greenhouse gas emissions to net zero by 2050, and the government's overall ambition is to leave the natural environment in a better state. Tax measures are an important tool in implementing environmental policy. Taxes can be levied on goods or services which harm the environment and thus incentivise businesses and people to change their behaviour. Tax reliefs can also encourage taxpayers to use environmentally friendly products or services. Tax measures can be used alongside other policy tools such as regulation to achieve environmental objectives.

Ministers decide on whether to use tax measures to support environmental goals. Where measures are used, HM Treasury and HM Revenue & Customs (the exchequer departments) are responsible for designing the measures to achieve objectives set by ministers, and for monitoring and evaluating their impact. HM Treasury is responsible for the strategic oversight of the tax system and HM Revenue & Customs ("HMRC") is responsible for administering the system.

HM Treasury and HMRC administer four taxes with explicit environmental objectives (referred to as environmental taxes throughout this report). Two are taxes on energy. The Climate Change Levy is paid by businesses and public sector organisations on consumption of energy through their energy suppliers. The Carbon Price Support is paid by electricity generators on the fossil fuels they use. The other two tax the disposal of waste at landfill sites (Landfill Tax) and the extraction of rock, sand and gravel (Aggregates Levy). These four taxes raised £3 billion in 2019–20. Other taxes, such as fuel duty (£28 billion in 2019–20), have an impact on government's environmental objectives but do not have specific environmental objectives.

Based on a report by the National Audit Office, the Committee took evidence on 8 March 2021 from the HM Treasury and HM Revenue and Customs. The Committee published its report on 28 April 2021. This is the Government response to the Committee's report.

Relevant reports

- NAO report: [Environmental Tax Measures](#) – Session 2019-21 (HC 1203)
- PAC report: [Environmental Tax Measures](#) – Session 2019-21 (HC 937)

Government responses to the Committee

1: PAC conclusion: HM Treasury has yet to set out how the tax system can help government achieve the UK's net zero target.

1a: PAC recommendation: HM Treasury should aim to become an exemplar finance department in supporting government's environmental goals like net zero;

1.1 The government agrees with the Committee's recommendation.

Target implementation date: Autumn 2021

1.2 HM Treasury is already playing an active role in supporting the government's environmental goals, including delivery of the legally-binding net zero commitment. As well as its role in relation to tax and spend policy and the financial services sector, HM Treasury is conducting an analytical review exploring the key issues and trade-offs as the UK decarbonises. Against a backdrop of significant uncertainty on technology and costs, as well as changes to the economy over the next 30 years, the Net Zero Review (NZR) focuses on the potential exposure of households and sectors to the transition, and its final report will highlight factors to be taken into account in designing policy that will allocate costs over this time horizon.

1.3 Work on the government's overall Net Zero Strategy is being led by the Department for Business, Energy and Industrial Strategy (BEIS), and HM Treasury is closely involved in developing this including to ensure that tax options are considered alongside regulation and spending.

1b: PAC recommendation: HM Treasury should by COP26 in November 2021, set out a clear vision of how it will work to help the UK achieve net zero.

1.4 The government agrees with the Committee's recommendation.

Target implementation date: Autumn 2021

1.5 Work on the government's Net Zero Strategy is being led by BEIS, and, as per the government response to the Committee on Climate Change's 2020 Progress Report, they will publish a comprehensive net zero strategy on behalf of the government ahead of COP26. This will set out the government's vision for transitioning to a net zero economy, making the most of new growth and employment opportunities across the UK.

1.6 It is not the role of HM Treasury to publish a separate strategy. Nevertheless, the NZR will include an update on how climate considerations are being embedded within HM Treasury governance arrangements, guidance and processes, including at fiscal events.

2: PAC conclusion: HM Treasury cannot explain how it will manage declining revenues from consumption of fossil fuels, worth £37 billion in 2019–20.

2: PAC recommendation: By the next Budget, HM Treasury should set out a timetable for how it will consult on options for replacing declining revenues from fossil fuels including fuel duty; and ensure it plans for sufficiently early and broad consultation with different parts of society, particularly with the government's levelling-up agenda in mind.

2.1 The government disagrees with the Committee's recommendation.

2.2 The government agrees on the need to consider the implications for tax revenue from net zero and the need over time to set out a plan for the replacement of fuel duty revenues but disagrees with the Committee's specific recommendation to set out a timetable before the next Budget, since that would pre-empt policy decisions which are for Ministers to take at the relevant time.

2.3 The [interim Net Zero Review report](#) in December 2020 highlighted that structural changes in the economy related to net zero will have fiscal implications. Much of the revenue from fossil fuel-based taxes is likely to be eroded during the transition to a net zero economy, the most significant of which are motoring taxes such as fuel duty. As set out by the Prime Minister in the Ten Point Plan for a Green Industrial Revolution, whilst the UK moves forward with the transition away from petrol and diesel cars and vans, the government will need to ensure that revenue from motoring taxes keeps pace with this change, so that the government

can continue to fund the first-class public services and infrastructure that people and families across the UK expect. The government will ensure it plans for sufficiently early and broad consultation with different parts of society.

3: PAC conclusion: We are concerned that immediate priorities have often outweighed action needed to support long-term environmental objectives.

3: PAC recommendation: HM Treasury should consider the pros and cons of publishing a roadmap that signals a clear trajectory to taxpayers for how tax measures will be deployed to contribute to net zero. It should write to the Committee to set out its thinking before the next Budget.

3.1 The government agrees with the Committee's recommendation.

Target implementation date: Autumn 2021

3.2 The government agrees to write to the Committee on the pros and cons of setting out a longer term roadmap on tax and net zero. It is not always appropriate for the government to pre-announce tax reforms given the issues caused by forestalling activity and wider market uncertainty. A standalone tax roadmap for net zero may also limit the strategic consideration and presentation of tax alongside regulatory and spending options. However, the government fully understands the importance of public engagement on tax policy and strategy. Any changes to tax policy are typically announced at fiscal events so that they can also be considered within the context of the tax system more broadly. In addition, where possible the government holds consultations on major tax reforms to support understanding of these measures.

3.3 Decisions on whether to publish a roadmap are a matter for Ministers.

4: PAC conclusion: Tax impact assessments do not sufficiently recognise the potential for every tax measure to affect progress towards environmental objectives.

4: PAC recommendation: From the next Budget, HM Treasury should:

- assess the environmental impact of every tax change considered; and**
- publish the expected environmental impact for each tax measure in the Budget, including the extent of behavioural change, alongside forecasts for tax receipts.**

4.1 The government disagrees with the Committee's recommendation.

4.2 The government agrees that it is important to consider the environmental impacts of relevant tax changes, but disagrees with the Committee's specific recommendation to assess, from Budget 2022, the environmental impact of every tax change considered and publish the outcomes. At this stage, it would not be practical, cost effective or possible to consider detailed environmental impacts for every tax change, such as any changes to the personal allowances for income tax or employer National Insurance Contributions.

4.3 The government does already carefully consider the environmental implications in relevant measures. For example, when considering reforms to the taxation of red diesel, the government assessed that in total red diesel accounts for the production of nearly 14 million tonnes of carbon dioxide a year. The [National Audit Office report](#) on environmental taxes highlighted that HM Treasury and HMRC 'use environmental data collected by third parties or feedback from stakeholders to assess impact and inform advice to ministers.' At Budget 2021, the government published an assessment of environmental impact of relevant tax measures - for example in the [Tax Information and Impact Note for Plastic Packaging Tax](#) which set out

that the tax was estimated to lead to around 40% more recycled plastic being used in 2022-23, saving nearly 200,000 tonnes of carbon dioxide.

4.4 The government will carefully consider next steps for options on internal assessment and publication of environmental impacts, taking into consideration the relevancy of environmental impacts to the tax measure. This will be kept under review in future Budgets. When deciding which taxes to focus on, the government must consider whether it is practical, cost-effective or possible to assess the environmental impacts, to ensure value for money for the taxpayer.

4.5 Decisions on the publication of information are a matter for Ministers.

5: PAC conclusion: HMRC has not done enough to evaluate how tax measures with environmental objectives have changed behaviour.

5: PAC recommendation: HMRC should ensure that it has sufficient information to assess whether environmental taxes are achieving their objectives and whether they are having wider impacts, including unwanted behaviour change.

5.1 The government agrees with the Committee's recommendation.

Target implementation date: Winter 2021

5.2 The government agrees it is important that HM Revenue & Customs (HMRC) should ensure it has sufficient information to assess the impacts of environmental taxes, including whether they are achieving their objectives.

5.3 HMRC already uses data and information from various sources to assess whether environmental taxes are achieving their stated environmental objectives and to identify and address unwanted behaviour and risks. For example, this led to the introduction of the Unauthorised Waste Sites measure to tackle non-compliance with Landfill Tax and wider waste sector regulatory requirements. HMRC is also building into the design of Plastic Packaging Tax mechanisms to support effective evaluation of its performance against stated environmental objectives.

5.4 Further activity will need to be considered within HMRC's overarching approach to evaluation and monitoring. Evaluation can be time consuming and expensive, so the evaluation plans will need to be proportionate, in order to appropriately direct taxpayers' money. And, as the NAO has recognised, it can be extremely difficult to disaggregate the impact of tax measures from other spending and regulatory measures, or other wider factors that drive the behaviour of individuals and businesses.

5.5 Decisions on publication of evaluation and monitoring information are a matter for Ministers.

6: PAC conclusion: We were concerned that HM Treasury and HMRC seemed to view the consequences of environmental taxes as the responsibility of other government departments.

6: PAC recommendation: The exchequer departments need to:

- consider and describe the expected impact of taxes on other departments' responsibilities for environmental objectives, for example within tax impact and information notes; and

- by autumn 2021, agree with other departments robust approaches for assessing and monitoring the effect of tax measures on government's environmental goals.

6.1 The government disagrees with the Committee's recommendation.

6.2 The government recognises that it is important to consider the impacts of taxes on environmental objectives and for HMRC and HM Treasury work closely with other departments to assess and monitor the impact of taxes. However, the Committee's recommendation could constrain the ability of Treasury Ministers to make decisions on the content of publications relating to tax policy in future Budgets. HM Treasury and HMRC already engage other government departments where it is appropriate in considering, formulating and managing policy, including tax policy that relates to environmental objectives, and will continue to do so. Whilst doing so the Exchequer departments have to take in to account the proportionality and practicality of further detailing of assessment and monitoring.

6.3 A recent example of such engagement is the Plastic Packaging Tax, in that it has been developed in tandem with wider waste policy reforms led by the Department for Environment, Food and Rural Affairs (DEFRA) and was decided on after considering a wide range of ideas to tackle plastic waste. Work also included cross departmental engagement between HM Treasury, HMRC and DEFRA to consider design issues with the new tax and interaction with planned DEFRA reforms and coordinating of consultations in 2019 on the high level design of the tax and waste reforms.

6.4 When considering the extent of this collaboration, HM Treasury and HMRC also have bear in mind the political and market sensitivity of tax decisions which are typically made and announced in Budgets to ensure coherency across the tax system.

6.5 The government will carefully consider next steps for options on internal assessment and publication of environmental impacts, taking into consideration the relevancy of environmental impacts to the tax measure and proportionality of which taxes to focus on to ensure value for money for the taxpayer. This will be kept under review in future Budgets.

6.6 Decisions on the publication of information are a matter for Ministers.