Road Traffic Taxation

Esko Linnakangas

1 Road Traffic Taxation in European Countries

1.1 Introduction

The taxation of road traffic comprises the consumption taxes related to the purchase and use of a motor vehicle. The taxes levied on the *purchase* are the *customs duty* and *value-added tax* to be paid on the vehicle as well as a *selective tax* (car tax), which resembles an excise duty. The road traffic taxes associated with the *use* of a vehicle consist of the *customs duty on fuel*, *excise duties* (excise duty on fuel), *value-added tax*, as well as a tax based on how long a vehicle is in use (*annual tax*).

In the past, *customs duties* were a central element in the taxation of road traffic, but their significance today is minor. Finland has been a member of the European Union since 1995, and no customs duties are levied in trade between member states. Member States apply a common customs tariff in importing goods from third countries.

With the exception of customs duties, highly significant differences in road traffic taxation can be found among the Member States of the EU. It is not possible to speak of a common European road traffic taxation. The present article focuses on *car* traffic. It draws to a considerable extent on the work Esko Linnakangas – Leila Juanto *Tieliikenneverot* [Road Traffic Taxes] (XXVIII + 693 pp.), published in 2000.

1.2 Value-added Tax

Although the content of *value-added taxation* in the EU has been harmonized to a significant degree, the tax rate still varies considerably. The general VAT rate, which is also applied to motor vehicles and the fuel used in them, must be at least 15% in the EU. The Nordic countries have the distinction of being those levying the highest rates. Value-added tax is particularly high in Norway,

© Stockholm Institute for Scandianvian Law 1957-2009

Sweden, Denmark and Iceland. The value-added tax rate in Finland is not among the very highest but it can nevertheless be considered rather harsh (as in Belgium and Ireland). France, Italy and Austria represent the average in this regard, with Greece, the Netherlands, Great Britain and Portugal applying distinctly lower rates. The countries having the lowest value-added tax rates are Spain, Germany, Luxembourg and Switzerland, with the rate being particular low in the last of these. It must be pointed out, however, that the deductions allowed in the value-added tax systems in different countries vary.

1.3 Excise Duty on Fuel

There are also considerable differences among European countries in the rate of *tax levied on fuel* (the EU has only prescribed a minimum rate that must be applied). In mid August of 2000, the tax on petrol was highest in Great Britain and lowest in Greece. In Finland, the tax on petrol is somewhat higher than average. Great Britain also has the highest tax when it comes to diesel fuel; the lowest rate is found in Greece, Luxembourg and Portugal. In Finland, the diesel tax is below the European average, and the difference between the price of petrol and diesel is large.

1.4 The Annual Vehicle Tax

The differences between EU states are even more striking in the case of what are known as non-harmonized taxes, i.e., the selective tax on the purchase of a vehicle (car tax) or the use-related, ownership-based tax on a vehicle (annual tax). Where these taxes are concerned, very significant differences indeed can be found in not only the tax rate but also the basis on which the tax is levied.

In some states, the annual tax on a petrol-powered car is calculated on the basis of the vehicle's *weight* (the Netherlands, Ireland and Sweden). A rather common criterion is the *volume* of the engine (Belgium, Spain, Greece, Luxembourg, Portugal and Germany). In certain countries, the *power* of the vehicle's engine is the decisive factor in determining the tax (France, Italy and Austria). The rate levied may be further affected by the *emissions level* of the vehicle (Germany and France). *Fuel consumption* may be an additional consideration (Germany) or, indeed, the sole criterion (Denmark). In several countries, the amount of tax levied also depends on the *age* of the vehicle (France, Portugal, and, to some extent, Finland). In some countries, the tax rate varies *regionally* within the country (the Netherlands, Spain and France). The crudest form of taxation on petrol-powered cars is found in countries (Finland and Great Britain) in which the tax is *fixed*; i.e., the same amount of tax is levied on all cars. In this last case, the tax basis is, in a sense, only the number of cars in the country.

Not only the tax basis but also the tax *rate* varies significantly for the annual tax in the different EU countries. The annual tax on an average new petrol-powered car is highest in the Netherlands. The rate is also quite high in Ireland

© Stockholm Institute for Scandianvian Law 1957-2009

and Denmark. Representing the average rate are Austria, Great Britain, Belgium, Italy, France, Germany and Iceland. The annual tax is comparatively low in Greece, Finland and Sweden, and very low in Luxembourg, Spain and Portugal.

1.5 The Selective Tax on the Purchase of a Car

Even more differences appear among the European countries when one examines the *selective tax on the purchase of a car* (car tax). There are EU countries in which such taxes *do not exist* (Italy, Luxembourg, France, Sweden, Germany and Great Britain). These countries count among the major car manufacturers.

In most EU countries (the Netherlands, Belgium, Spain, Ireland, Austria, Greece, Portugal, Finland and Denmark), as well as in the EEA countries of Iceland, Norway and Switzerland, a selective tax is levied on the purchase of a car. In some countries, this tax is based solely on the *technical features* of the vehicle. In Portugal, the crucial criterion is the piston displacement of the engine; in Belgium, this and the power of the engine are both taken into account; In Norway, both criteria are used but are complemented by a third consideration, the weight of the vehicle.

In some countries, it is both the piston displacement of the engine and the value of the car that affect the amount of tax levied (Spain, Ireland, Iceland and Greece). In Greece, the level of emissions also has a significant impact on the tax. In Austria, the tax is determined on the basis of the vehicle’s fuel consumption and value. In some countries, the car tax depends exclusively or almost exclusively on the *value* of the vehicle; these include the Netherlands, Finland, Switzerland and Denmark. In Finland, the tax is also affected by the emissions level (deduction for catalytic converter). In Denmark, a range of safety equipment (e.g., air bags and non-locking (ABS) brakes) also has bearing on the amount of tax levied.

Even where the tax value of a vehicle affects the tax levied on it, considerable differences obtain in how that value is defined. In the Netherlands, the tax value is the net list price; in Spain, the value is determined as for value-added tax. In Ireland, the market value is used, in Iceland the customs value, in Austria and Switzerland the invoice price, in Greece the wholesale list price, in Finland the purchase price, and in Denmark the general retail sales price.

Substantial differences can be seen not only in the basis for determining the tax but also in the *tax rate* applied. Denmark is in a class by itself in this comparison, followed by a group comprising Greece, Finland, Norway, Portugal and Ireland. Falling in the middle are the Netherlands and Iceland. Rather light taxation can be found in Austria and Spain, and extremely light in Switzerland and Belgium.

The differences in the retail prices of cars among countries are not nearly as great as one might assume after examining the varying amount of tax levied. This is due to the fact that car manufacturers often sell vehicles at a lower price to countries which have a high car tax than to countries where there is either no tax on the purchase of a car or the rate is extremely low.

© Stockholm Institute for Scandianvian Law 1957-2009

2 The Objectives of Taxation

The central objective of taxation is a *fiscal* one; i.e., taxes are designed to generate revenue for the public sector. Now that Finland is a member of the European Union, one must distinguish between taxes levied to meet that country's own revenue needs, on the one hand, and the needs of the EU on the other. Revenue obtained from customs duties are EU revenues. However, of even greater importance to the financing of the EU are the fees subject to VAT that are collected by Member States. Road traffic taxation in Finland and many other countries is of extreme importance fiscally.

One of the central principles in taxation is consideration of ability to pay tax. This principle is also connected with the fiscal objectives of taxation. The emphasis on the *ability to pay tax* where consumption taxes are concerned has been linked with the *luxury tax* approach, but luxury taxes are rarely mentioned any longer, at least in connection with road traffic. The fact that taxation of cars in Finland is dependent on the price of the vehicle and is (slightly) progressive in nature accords well with the principle of ability to pay tax. Road traffic taxation also exhibits certain other *socio-political* features, such as the system of car tax refunds for the handicapped. For its part, the special consideration given to antique cars can be seen as furthering *cultural policy*.

Taxation is also used as a means of *guiding society*. This guidance is indirect, taking the form of decisions made by the taxpayers. When the means used to effect guidance is lighter than average taxation, we may speak of tax support. The reverse is a tax sanction. The Finnish road traffic taxation system includes taxes which can be regarded as rather straightforward *tax sanctions*. The vehicle surtax and fuel fee are taxes which fulfil their purposes better, the less tax revenue they generate. In fact, they have been enacted mainly to ensure that diesel-powered vehicles are not run using light fuel oil; in other words, their objective is to ensure collection of another tax.

Road traffic taxation in Finland had strong elements of guidance particularly in the 1960s and 1970s. When one considers the fact that taxes make up almost half the price of a car, substantial changes in taxes have a strong impact on the prices of, and, at least in the short term, the demand for cars. The car tax has also been used to *regulate foreign trade*. The proportion of taxes in the price of fuel is highly significant; fully three-fourths of the price of petrol is tax. Changes in the taxation of fuel have occasionally been used to keep the price of fuel stable, for example.

Discussions of road traffic taxation generally bring up the issues of the costs to society of traffic and who should pay those costs. Where taxation of the use of motor vehicles is concerned, a topic that has come up since as far back as the 1920s is the *cost of building and maintaining the road network*, although the question is one of taxes and not road tolls.

Much later - since the early 1970s or so - questions of *traffic safety* have become prominent. This has been seen particularly in forms of car taxation in which certain types of safety equipment have been given special treatment when determining the tax value of a car. The present tax system in Finland does not

© Stockholm Institute for Scandianvian Law 1957-2009

have any noteworthy traffic safety incentives; normative guidance is regarded as a more effective means to this end.

Since the beginning of the 1980s, the *environmental problems* caused by road traffic have been increasingly focal concerns in the discussion of road traffic taxation. Traffic, and the pollution it causes, constitute one of the most serious global environmental threats. Tax provisions can have an impact on the number of vehicles and the amount of driving done as well as on consumers' choice of vehicle and fuel. The guiding influence of the general tax rate on a particular mode of transport can be combined with individual incentives and sanctions. In Finland, as elsewhere, tax provisions have hastened the transition to cars with catalytic converters as well as to the use of more "environmentally friendly" petrol and diesel.

In summer 1998, the EU Commission published a White Paper on Fair Payment for Infrastructure which proposed that pricing be harmonized in different modes of transport in order to achieve a system of pricing that would be fair and efficient. The proposal endorsed the "polluter pays" principle.

3 The Origin and Development of Road Traffic Taxes in Finland

3.1 The Selective Tax on the Purchase of a Car

3.1.1 The Origin and Development of the Tax Prior to Finnish Membership in the EU

In Finland, the taxation of cars when purchased began as a form of customs duty. The first cars were imported into Finland in the very early 1900s but cars did not start becoming common until after independence in 1917. Although customs duties have been used to guide the import of cars, the principal function of the duties has always been fiscal, i.e., the collection of tax revenue for the state.

The selective tax on the purchase of cars, the car tax, dates from the 1950s. Starting in 1953, an equalization fee was levied on cars and motorcycles and placed in a *price equalization fund*. The aim of the equalization procedure was to keep the sales prices of vehicles constant regardless of the forms of trade or price of the currency that had to be used in purchasing the vehicles at any given time. The price equalization of motor vehicles was also designed to avoid there being excessively large differences between the officially established prices and the prices charged for vehicles that had been obtained by other than motor vehicle importers proper or for vehicles that had been little used. In addition, the fund that accrued from the equalization fees made it possible to reduce the prices of certain accessories which were considered important for pricing policy.

As import trade became increasingly liberalized and changes in currency exchange rates occurred, the price equalization procedure was scaled back, and the Finnish economy was developed in the direction of more stable circumstances. However, the state of the national economy at the time made it impossible to give up the revenue which the equalization fees had brought in. Moreover, as the importing of cars and motorcycles was restricted, it was not

© Stockholm Institute for Scandianvian Law 1957-2009

considered reasonable to let the established prices decline to any substantial extent, because this would have increased opportunities for speculation. Accordingly, the Government submitted a bill to Parliament on 22 November 1957 proposing that the equalization fee procedure be replaced by a separate car and motorcycle tax.

Parliament approved the bill with certain modifications and the Act came into force on 1 January 1958. In approving the Act, Parliament required that the tax be temporary, motivated only by the particularly serious financial situation of the state at the time, and that efforts be made to eliminate the tax, especially for the lowest priced vehicles, as soon as the state economy permitted. This opportunity has apparently not presented itself in the last 40 years.

A new Act was enacted in 1961 that was essentially the same as the previous one. It was soon replaced, in the summer of 1962, with a new, substantially harsher Act. The central features of the new legislation were that it *raised* the car tax markedly and made the tax a *progressive* one. The tax was proportionately highest for the most expensive cars. The purpose of the tax increase was to distribute the pressure to buy cars over a number of years now that the importing of cars was no longer regulated. The Government's reasoning as presented in the bill was that the changes took into account aspects of trade policy and interests linked to bilateral trade.

The year 1966 can be seen as marking a new phase in the history of car taxation in Finland in light of the scale of the car tax *increase* implemented in the middle of that year to alleviate problems in the balance of payments. The tax was raised further in the beginning of 1967 in order to compensate for the decline in tax revenues following the reductions in EFTA customs duties.

In the autumn of 1967, soon after a major devaluation, the Government submitted a bill for a wholly new car and motorcycle tax. The new Act came into force on 15 November 1967. The amount of car tax was reduced in order to offset the rise in car prices resulting from the devaluation. As it was expected that a large number of used cars would begin to be imported into the country, the tax on used cars was set at a level almost equal to that of the tax on new ones.

In 1969, it was prescribed that the tax value of a car or motorcycle manufactured in Finland was the price of the vehicle at the place of manufacture as determined by the *manufacturing costs* of the vehicle. The matter had started to become increasingly important with the beginning of mass production of cars in the country.

In the 1970s, *traffic safety* took on a growing importance in car taxation. At the end of 1970 and the beginning of 1971, the law defined a seatbelt as a piece of equipment whose value was not to be included in calculating the tax value of a car.

The year 1971 saw one of the truly crucial changes in the history of car taxation in Finland, as the tax exemption for vans was restricted to vehicles whose storage space fulfilled certain minimum dimensions. Only rather large, box-model vans generally qualified for the exemption. Following the new legislation, the import of vans dropped sharply. At the end of 1973, the tax on motorcycles, especially large ones, was raised. This was justified primarily in terms of traffic safety.

© Stockholm Institute for Scandianvian Law 1957-2009

The Oil Crisis at the end of 1973 raised the price of energy appreciably. The impact of the increase for those operating a vehicle as part of their profession was offset at the beginning of 1974 by an amendment whereby the car tax on a vehicle used for professional purposes could be refunded in full up to a certain amount. Among the reasons for the change was that it encouraged a shift towards *longer lasting and more energy efficient vehicles*. The desirability of this trend was underscored with references to considerations of *energy and environmental protection*.

The number of new cars in importers' stocks rose considerably by autumn of 1975, and it was at that time that strong measures were taken to limit imports and maintain the balance of payments. A number of decrees issued pursuant to an Act designed to safeguard the country's foreign trade and economic growth imposed a special fee on the import of cars and motorcycles.

Car taxation in Finland has been more stable since 1976. At the beginning of 1977, it returned to its "normal" level. At the same time, the tax on motorcycles was reduced substantially from what it had been during the previous few years.

An amendment which came into force in the beginning of 1978 assigned a clearly greater importance to *traffic safety* than it had been given theretofore. The legislation dealt with equipment which was not to be taken into account in calculating the tax value of a car. The provisions in question were also drafted so as to *favour Finnish production*.

The beginning of the 1980s can be described as a period of fine-tuning when it comes to taxation. For example, amendments were enacted which were intended to prevent importing of new vehicles that were "over-aged" or the importing of vehicles damaged in accidents and parts from them.

Changes in the legislation on car taxation in the mid 1980s and thereafter pertained to, among other things, the simplification and clarification of taxation and lowering the tax rate. When the tax base was lowered, the law was changed such that safety equipment, with some exceptions, was taken into account directly in the formula for calculating tax, with deductions no longer being allowed when determining the tax value. Amendments were also enacted easing taxation on vehicles 25 years or older. The end of 1988 brought enactment of a new provision where *environmental policy* was concerned, i.e., a deduction for a catalytic converter in the taxation of low-emission petrol-powered cars.

The car tax was lowered on 1 September 1990 in order to reduce the consumer prices of cars. This was done by decreasing the factor in the formula used to calculate the tax. In order to shift the focus of road traffic taxation towards taxation of use and to promote employment in the auto industry, the car tax rate was again lowered on 25 May 1991. A more substantial reduction occurred in May of 1993. Following the latter, the tax was 102% of the tax value (before a 4600 FIM deduction). The reduction in tax was intended to both relieve pressures to increase the consumer price of cars and to *shift the focus of road traffic taxation towards use*. Related to this same amendment was the introduction of the annual vehicle tax, or what is known as the car use tax.

While the car tax was lowered at the beginning of the 1990s, the trend in the case of vans was the reverse. In order to prevent what had become widespread speculation, in 1990 the technical requirements for receiving a full tax

© Stockholm Institute for Scandianvian Law 1957-2009

exemption were tightened. In 1993, tax exemption for vans was discontinued and the tax base was set at 35% of the vehicle's tax value.

3.1.2 Car Tax in EU Finland

At the beginning of 1995, the Act on Car Tax (29.12.1994/1482) came into force, which replaced the previous Act on Car and Motorcycle Tax. Enactment of the new legislation became topical following Finland's accession to the EU. The country had to change over to a system in which taxation was no longer implemented in conjunction with border formalities.

The principal changes introduced had to do with the liability to pay tax, the determination of tax value and the dates for debiting tax. The general tax rates at the time remained the same. The 1.5% deduction that had previously been granted as a protective buffer was removed, and the normal tax percentage was reduced accordingly. Thus the tax was prescribed as being the tax value minus 4600 FIM, or 770 € The deduction for a catalytic converter was retained unchanged.

The full tax exemption for a vehicle brought into the country by a person immigrating (a removal car) was discontinued. A change was effected to a system in which a specific ceiling was set on the tax reduction. The range of persons entitled to this reduction was also reviewed. New provisions were introduced into the Act pertaining to used vehicles imported into the country; these were intended to create a system which "just barely" fulfilled EU requirements.

The Act on Car Tax has been amended numerous times. Of its some 100 sections, only half remain in their original form. Most of the amendments have been technical adjustments of relatively little significance. Those of more substance include the regulation on removal cars. The more recent changes in the legislation pertain to the import of cars and are consequences of the letter of formal notice which Finland received from the Commission of the EC. The car tax in Finland is still problematic from the point of EC Law, however.

3.2 Origin and Development of the Annual Tax

Fixed taxation based on the use and ownership of a car began in 1922 with a tax levied in keeping with the Act on Stamp Duty. The tax yielded rather little revenue. Taxation was reformed in 1929 by enacting a separate Motor Vehicle Act. The reform emphasised that the motor vehicle tax was to be based not on luxury tax but more on considerations of *road economy*. An effort was made to see to it that the bases on which the tax was determined were, as a rule, factors describing the impact of a vehicle on the roads, in particular its weight. A higher tax was levied on vehicles which did not have pneumatic or other rubber tires on their wheels.

According to the bill, the revenue from the tax was to be used to improve and maintain public roads. However, on a proposal by the Select Committee on

© Stockholm Institute for Scandianvian Law 1957-2009

Finance this condition was removed. In the Committee's opinion, the Parliament should have the freedom to decide on how this revenue, like any other, was to be used, particularly as the state's annual expenses for roads at that time were significantly greater than the anticipated revenues from the tax at issue.

The *late 1930s* saw a transition to a new phase in the motor vehicle tax. In road traffic taxation, the customs duties on the petrol used by a vehicle had been more important than the tax on the vehicle. A vehicle's consumption of fuels was also seen as indicating the wear on the roads it entailed. However, the system of road traffic tax started to become distorted with the introduction of vehicles using fuel that carried no or low customs duties, such as *diesel-powered lorries and buses*. As the fuel used in these vehicles could be used for many other purposes as well, it was not considered possible to tax the fuel directly. The solution adopted was a surtax based on the distance travelled in the diesel or other vehicle. Determining this was difficult. Since it was not practicable to check odometers, imposition of the tax was often a discretionary procedures that was based on the driver's log. Accordingly, *at the end of the 1940s*, a system was introduced in which the surtax on diesel and other vehicles was a fixed sum based on the *average number of kilometres driven in different types of vehicles*.

The tax on petrol-powered vehicles was low, and the focus of the tax was on fuel. *At the beginning of 1965*, a significant structural reform of the motor vehicle taxation was implemented: *the vehicle tax proper was discontinued for petrol-powered vehicles and the excise duty on petrol was raised correspondingly*. Thus the motor vehicle tax was levied only on vehicles using other fuels, i.e., *mainly diesel-powered cars*. The tax is generally referred to as the diesel tax. The *surtax* was levied on vehicles when the fuel used in them was tax-free or only lightly taxed fuel that use of the vehicle did not require as such, e.g., light fuel oil in the case of a diesel car. The structure of the motor vehicle tax has remained essentially the same, although some details have been modified.

In 1993 the Act on the *Fuel Fee* was enacted (337/1993), which is connected with motor vehicle taxation and, in particular, the surtax. The fuel fee is intended to prevent the use of light fuel oil instead of diesel oil in both domestic and foreign cars.

In 1976 a special *use fee* was levied on cars registered in Finland. The fee was motivated by the economic situation of the country at the time. Persons subject to the fee purchased a *use-fee sticker* which corresponded to the sum to be paid and was obtained from the post office or customs office and affixed to the vehicle. The idea was to create a system that was simple administratively. The fee was levied in 1976 only. However, a similar system was introduced in the 1990s.

In presenting a bill in the spring of 1993 amending the Act on Car and Motorcycle Tax, the Government included a statement in the record of the Government meeting to the effect that the reduction in car tax revenues caused by the amendment was to be compensated for by the introduction of an annual tax on all cars.

The car tax was lowered approximately one fifth, and to compensate for the lost tax revenues, the Act on the Vehicle Tax on Certain Vehicles was enacted. The Act stated that the tax was to be levied through a tax sticker to be affixed to

© Stockholm Institute for Scandianvian Law 1957-2009

the vehicle. Payment of the tax required the owner or possessor of the vehicle to obtain the sticker on his or her own initiative and to affix it to the vehicle. Supervision of payment was based on the sticker's being visible in traffic supervision as well as the fact that a vehicle lacking a sticker could not be approved in inspection. Use of a vehicle without an appropriate sticker resulted in the user's no longer being allowed to operate the vehicle.

The tax was criticized for a variety of reasons. That the users themselves had to buy the sticker and attach it to the windscreen was considered an inconvenience to them, particularly as they had to remove the old sticker. The way in which stickers had to be obtained was also criticized.

Parliament demanded that the Government take measures to collect the vehicle tax also for periods less than one year and to implement a system of refund and tax exemption for vehicles used by handicapped persons. In 1996, the Ministry of Finance in fact set up a working group to ascertain the advantages and disadvantages of the ways in which the vehicle tax was collected as well as to determine viable alternative procedures. The working group was to pay particular attention to the arrangements by which handicapped persons or vehicles used by such persons could be exempted from taxation.

The working group reviewed seven alternatives for collecting the equivalent tax revenue, primarily on cars and vans. It considered the most flexible option to be a change from tax collected through a sticker to tax collected through a *tax notice* posted to those liable to pay. It was this recommendation that then formed the basis for the bill on motor vehicle tax presented by the Government in 1996. The bill proposed that from the beginning of 1997 the tax be collected using notices instead of stickers. The principal objective was to make best use of existing techniques for collecting taxes and computer applications.

Parliament accepted the government's proposal with very minor modifications. The Act on Motor Vehicles (20.12.1996/1111) came into force in 1997. The Act was amended, effective as of the beginning of 1999, in that tax could be refunded to a taxpayer if the vehicle was removed from the register during the tax period.

Revenue from the motor vehicle tax has thus been used to cover losses in tax revenue from taxes related to the purchase of a vehicle, i.e., the car tax. The *fiscal goal* in this case is related to the shift in the focus of road traffic taxation from the purchase to the use of a vehicle. The link to car taxation can be seen in the fact that, for the most part, the scope of the car use tax includes vehicles similar to those in car taxation: in both instances buses and lorries are exempt from taxes.

As a form of taxation, the car use tax is still a crude way to tax the use of a vehicle, because the amount of tax for vehicles falling within its scope is generally the same regardless of the number of kilometres driven or the weight of the vehicle, for example. This tax is far less sophisticated that the tax on fuel and the motor vehicle tax proper (the so-called diesel tax) when it comes to taking environmental concerns into account. Yet even the present vehicle tax is very rough when compared to the taxes associated with the purchase of a car. It does not, for example, take into account the value of the car - an indication of the user's ability to pay tax which is of central importance in the taxation related

© Stockholm Institute for Scandianvian Law 1957-2009

to the purchase of a car. The inflexibility of the tax is also seen in its applying to types of vehicles which are exempt or receive some relief from car tax (e.g, ambulances, taxis for the handicapped, hearses and campers).

The reform of motor vehicle taxation that came into force in 1997 has no specific traffic- or environment-related objectives. The annual tax increases the proportion of costs that do not vary with the number of kilometres driven, which cannot be considered a favourable development in terms of environmental or traffic policy; however, the reform did not change the prevailing situation.

4 Reforming Road Traffic Taxation in Finland

The greatest legal pressures for reforming road traffic taxation in Finland have to do with the *car tax*. Although the tax is basically a national one, Finland is not entirely free to decide its content, for like many other taxes, the car tax may not violate EU Law, in particular the *prohibition against discrimination*. Numerous complaints have been filed with the Commission, and the European Court of Justice is currently (summer 2002) considering a reference from the Finnish Supreme Administrative Court for a preliminary ruling. The issue to be clarified is whether car taxation in Finland is discriminatory in that the tax varies depending on the level of distribution, i.e., whether the person liable to pay tax is a wholesale enterprise, a retail enterprise or a consumer. The problem pertains to used and new vehicles alike.

If the level of distribution is deemed to be discriminatory (as the opinion of the Advocate General indicates) it is likely that it will be necessary to discontinue basing the car tax on the vehicle's purchase value, a practice which has many traces of import taxation (customs taxation). What remains will be the option of basing the tax on a car's technical features or general retail sales value. At the present, high rate of taxation, basing the tax on technical features would entail such great changes in the relative tax burdens of vehicles that this is hardly a viable approach. There is hardly any other alternative in the short run than to use a vehicle's *general retail sales value* as the basis for the car tax on new vehicles (models for this are found in the Netherlands, Ireland and Denmark), with it being prescribed by law that the amount of tax be public knowledge. This would clearly also satisfy the requirement that taxation should be transparent. Determining the general retails sales value entails problems of its own, however.

The level of car taxation in Finland at present is comparatively high in international perspective, and there is no obstacle in EU Law to retaining this level regardless of potential changes in the basis for the tax. Present levels of tax revenue can be collected in the future through the car tax if desired. If the car population is to be replaced with vehicles in which environmental and safety factors are better taken into consideration than at present, then arguments can be found for *lowering the car tax rate*. Given the present state of the Finnish economy and the risk of market disturbances, it is highly unlikely that a single substantial reduction could be effected; rather, the reform would have to be implemented through a series of decreases.

Reductions in the car tax rate are often opposed using the argument that reducing the tax would not result in lower consumer prices. The reasoning here

© Stockholm Institute for Scandianvian Law 1957-2009

is that manufacturers would raise the tax-free prices of the cars sold to Finland, which are generally low for Finland and other countries where the car tax is high. However, it is likely that the factory prices of cars supplied to different countries will eventually level out because EU Law entitles consumers to purchase their vehicle in any country in the EU. The tax on *used vehicles* In Finland may also in the future be linked to the general retail sales value of the vehicle, either rather crudely or in a more particularized fashion.

If the reduction in the car tax is to be compensated for by raising other road traffic taxes, one must take into consideration that the fuel tax in Finland is at present high. In international perspective, the principal opportunity for raising taxes lies in the *annual motor vehicle tax*. It would be consistent to raise the tax on vehicles which fall within the scope of reductions in the car tax, although the tax compensation would accrue very slowly. In fact it is possible that it will become necessary to raise the motor vehicle tax on old, heavily taxed vehicles. This could also be justified on environmental grounds. In reforming the annual vehicle tax, there is also clearly good reason to *graduate the tax* according to the quality of the vehicle as well. It can be prescribed that the amount of tax levied is to depend on, for example, the mass of the car, the piston displacement and fuel consumption of the motor, or the level of emissions.

The foregoing treatment has examined the pressures for the development of road traffic in Finland primarily from the legal point of view. This vision does not change appreciably, however, even in broader perspective. For example, the Action and Economic Plan for the Ministry of Transport and Communication for the period 2001-2004 states, among other things, that the Ministry considers it important that road traffic taxation be used more as a means for the economic guidance of traffic policy in addition to its fiscal aims. Taxation can influence the number of vehicles on the road and the structure of the vehicle population. This in turn has an impact on energy consumption and traffic safety. Moreover, the taxation of fuels can promote the development and introduction of more environmentally friendly fuels. Taxation can thus check the rise in external costs even if the amount of traffic increases. The Ministry's goals for the reform of the tax structure of car traffic are the following:

1. Reforming and lowering the taxation of the purchase of new cars and, at the same time, giving due consideration to the taxation of the importing of used cars; the goal is to promote an increase in the proportion of environmentally friendly cars with low fuel consumption.
2. Graduation of the annual taxes on the basis of environmental factors; in the short term the vehicle tax for old and new cars should be the same, and, in the long term, the amount of tax levied should be based on fuel consumption or other features, for example.
3. The level of fuel taxation should be kept stable; however, there should be continued restriction of the technical features that serve as the basis for forms of tax relief.

The system of road traffic taxes has been examined *in the longer term* in a working group report published by the Ministry entitled *Väyläpalvelujen*

© Stockholm Institute for Scandianvian Law 1957-2009

rahoituksen uudet mallit (6/2002) [new models for financing roads]. In the view of the working group, in the 2010s Finland should change over to a system comprising a two-part road traffic use fee containing a variable and a fixed component that would replace the tax-like use fee. There would be a clear connection established between the costs involved and the fee, whereby the person paying the fee would know what he or she is paying for. The variable fee should depend on traffic use, axle weight and, if technology permits, also *the place and time of use of the vehicle*. In the opinion of the working group, the proposed model would effectively address the challenges posed by national traffic policy and sustainable development. The solution would implement the goals of EU pricing policy and, as a pioneering approach, would offer an opportunity to influence the content of that policy. Pricing based on location would, in the group's view, also offer new opportunities for regional and local pricing and, accordingly, further the development of the traffic system and the structure of the community. The solution would also promote traffic safety. Underpinning the working group's proposal is the assumption that the new fixed and variable fees will replace the earlier fiscal taxes without significantly changing the tax burden on the user of traffic.

The model advanced in the report presupposes considerable technical development. The model is also not a politically realistic one in today's perspective; indeed, a number of dissenting opinions are on record. Moreover, the legal problems involved have yet to be clarified.

© Stockholm Institute for Scandianvian Law 1957-2009