EXPLANATORY MEMORANDUM TO

THE CLIMATE CHANGE LEVY (SUSPENSION OF TRANSPORT EXEMPTION) ORDER 2011

2011 No. 1025

1. This explanatory memorandum has been prepared by HM Revenue and Customs on behalf of HM Treasury and is laid before the House of Commons by Command of Her Majesty.

2. Purpose of the instrument

2.1 This Order suspends the exemption from the climate change levy in respect of taxable commodities (principally electricity) supplied for use by open access rail services and rail freight.

3. Matters of special interest to the Select Committee on Statutory Instruments

3.1 This Order has been made in exercise of a power contained in a House of Commons resolution passed on 29 March 2011, which has temporary statutory effect by virtue of section 1 of the Provisional Collection of Taxes Act 1968. Provisions corresponding to those in the resolution appear in clause 79 in the Finance (No. 3) Bill 2011 published on 31 March, and, provided the clause is not rejected during the passage of the Bill through the House, will be given permanent effect on Royal Assent. The Order made under the resolution will continue to have effect by virtue of those provisions of the Act arising from the Bill.

3.2 It has been necessary to breach the 21-day rule because it was not possible to make the instrument until after the resolution conferring the power to make it was given temporary statutory effect at the end of the Budget debates. As explained at paragraph 7, it is necessary for the Order to come into force on 1 April 2011 in order to avoid a breach of European law.

4. Legislative Context

4.1 Paragraph 12 of Schedule 6 to the Finance Act 2000 provides for taxable commodities used in certain forms of transport to be exempted from the climate change levy. The exemption qualifies as a State aid and was approved by the European Commission until 31 March 2011. Since this approval was granted the legal frameworks relating to State aids have changed. Consequently, as far as the transport exemption is concerned, only two specific categories of rail operator – open access services (as defined in the Order) and rail freight - require explicit Commission approval. The Government is pursuing a further 10-year

period of re-approval for these rail services. Approval is expected shortly, but it will not have been received by 1 April 2011, when the current approval will expire. The Government therefore needs to suspend the exemption until that approval is obtained, in order to remain compliant with EU law.

4.2 The exemption for the bulk of UK electrified rail services (and similar public transport) do not require Commission approval and the legislation in paragraph 12 relating to these services remains unchanged.

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

Although this Order is subject to negative resolution and does not amend primary legislation, it does affect the interpretation of primary legislation, so human rights have been considered.

The Economic Secretary, Justine Greening, has made the following statement regarding Human Rights:

In my view, the provisions of the Climate Change Levy (Suspension of Transport Exemption) Order 2011 are compatible with the Convention rights.

7. Policy background

- ***What is being done and why***

7.1 When the climate change levy was introduced in 2001 a number of exemptions were included for various policy reasons. One of these exemptions was for taxable commodities used in certain forms of transport. In practice the principal beneficiaries, in terms of the monetary value of the exemption, are electrified rail based public transport services, such as the electrified parts of the national rail network and London Underground. The exemption qualified as a State aid and required the approval of the European Commission. The current period of approval will expire on 31 March 2011.

7.2 The policy reasons for exempting these forms of transport remain. Electrified rail based transport continues to be one of the lowest carbon forms of mass transport, and a continued exemption will help to support this mode of travel. The Government has therefore sought a further period of State aid approval. The Commission has now informed us that the bulk of the public transport rail services concerned would be covered by a simplification Regulation passed in 2007 and the exemption for these services does not require approval from the Commission in order for it to continue. However, the simplification

Regulation does not apply to the transport of goods by rail (rail freight), or to public passenger transport service providers not subject to public service obligations (which the Order refers to as "open access services"). The exemption for these services does therefore require Commission approval. The Government is optimistic it will receive an approval shortly, but this will not be before 1 April 2011, when the existing exemption expires.

7.3 In order to remain compliant with EU law and avoid the risks associated with the exemption becoming an illegal State aid, it is necessary to suspend the exemption as it applies to rail freight and open access services. The exemption will be reinstated for these service providers if State aid approval from the Commission is forthcoming and it will be reinstated retrospectively if the terms of the approval allow. In these circumstances taxpayers would be entitled to reimbursement of any levy paid during the period of suspension.

- ***Consolidation***

7.4 The Government does not intend to consolidate the legislation at this time.

8. Consultation outcome

8.1 The Government has informally consulted the representative bodies for the various transport sectors concerned. There is strong support for a continued exemption and the case for it is sound. The Government is optimistic that the case put to the Commission will secure approval where this is required. The representative bodies have been advised that the exemption might need to be suspended pending the European Commission's decision and there was no adverse reaction to this.

9. Guidance

9.1 HM Revenue & Customs wrote to the representative bodies for rail freight and rail passenger services on 9 March 2011 advising what action their members should take if the exemption was suspended. The department's published guidance has not been amended at this stage because it is expected that the duration of the suspension will be short.

10. Impact

10.1 The impact on business, charities or voluntary bodies is negligible.

10.2 There will be no impact on the public sector.

10.3 A Tax Information and Impact Note covering this instrument was published at Budget on 23 March 2011 and is available on the HMRC website at www.hmrc.gov.uk/budget2011/tiin6840.

It remains an accurate summary of the impacts that apply to this instrument.

11. Regulating small business

11.1 The legislation applies to small business.

11.2 To minimise the impact of the requirements on firms employing up to 20 people, the approach taken is a general tax provision and the same for all firms.

11.3 No concerns regarding the impact on small businesses have been expressed by the representative bodies.

12. Monitoring & review

12.1 The nature of the instrument is such that there is no requirement to monitor or review its impact.

13. Contact

Andy Jameson at HM Revenue and Customs Tel: 020 7147 2379 or email: andy.jameson@hmrc.gsi.gov.uk can answer any queries regarding the instrument on behalf of HM Treasury.