

LeasePlan Consultancy Services

Diesel briefing

2016



It's easier to leaseplan

1. Introduction

In April last year, Britain's Supreme Court ruled that the Government should do more to curb air pollution. More specifically, they wanted politicians to draw up a plan for reducing nitrogen dioxide (NO₂) emissions, which have been in breach of European Union standards for six years running. Given that NO₂ is especially a by-product of diesel engines, many commentators thought that this plan would heavily impinge on diesel vehicles and their drivers.

A lot has happened around diesel in the year since then. The cost of the fuel itself has fluctuated such that, for a couple of months last summer, it was even cheaper than petrol. The market share of new diesel cars has fallen by almost two percentage points. And companies such as Volkswagen have faced questions and criticisms over how they test the emissions of their diesel vehicles.

But, amid it all, what has our Government done to satisfy the Supreme Court's demands? Their most noticeable extant policy, particularly for us in the leasing industry, has been the extension of their diesel surcharge. This three percentage-point addition to the rates of Company Car Tax (CCT) paid by diesel motorists was meant to be phased out at the beginning of April. Instead, in his most recent Autumn Statement, George Osborne revealed that it will remain for another five years.

This abrupt decision has burdened motorists with costs that they didn't expect. It is a bad way of doing policy. But, thankfully, not all of the Government's measures have been like this. Their support for ultra-low emission zones is an admirable way of encouraging people to choose cleaner cars.

In fact, it's so admirable that, as Parliament's Environment, Food and Rural Affairs Committee recently suggested, it should probably be extended more quickly.

Aside from these policies, the Government has not yet done as much as we might have expected. There was speculation that the entire system of CCT could be based on NO₂ emissions instead of, as it currently is, carbon dioxide (CO₂) emissions. Yet, in his latest Budget, the Chancellor confirmed that CO₂ will remain the determinant of tax rates from now until 2021 and beyond.

But could bigger policies be on the way? Perhaps. In a recent interview, the Transport Secretary Patrick McLoughlin suggested that previous governments had, in hindsight, been wrong to incentivise the purchase of diesel vehicles. 'It is something the Chancellor will need to look at in due course,' he said.

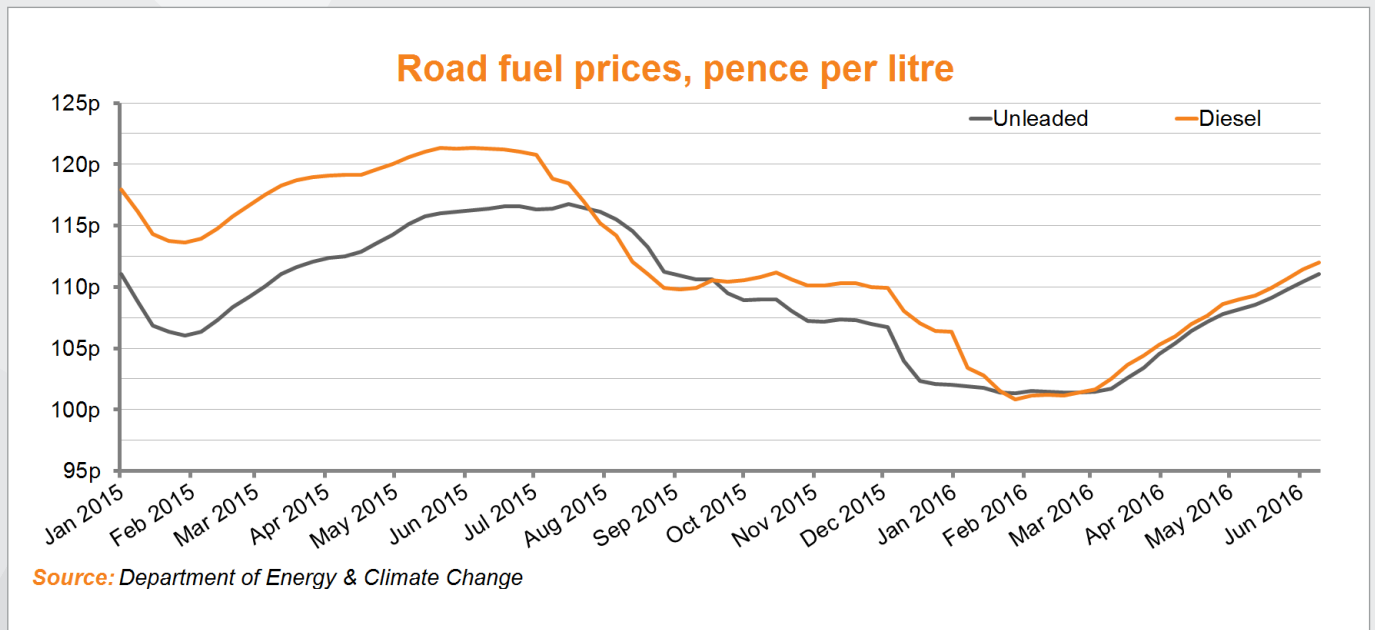
LeasePlan is eager to help its customers prepare for the possibilities, which is why we have produced this briefing document. It isn't meant to be a comprehensive account of everything that is going on in the world of diesel policy, but it does summarise what many of the main participants are saying and doing – from the Government itself to various industry bodies and think-tanks. It will enable fleet managers to make more informed decisions.

And fleet managers do have decisions to make. Is diesel still viable? Is ultra-low the way to go? What are the costs associated with new technologies? As during any period of great change, the answers may take some time to emerge. In the meantime, we at LeasePlan see it as our responsibility to provide as much clarity as we can.



2. The marketplace

The price of diesel



The price of diesel, like the price of petrol, has fluctuated with the underlying cost of the crude oil that goes into its production. Around a year ago, as our graph shows, a litre of diesel cost about 121 pence at the pumps. At the turn of this year, it was closer to 100p. It now stands around 112p.

There have even been occasions, most notably last summer, when the price of diesel has been lower than the price of petrol – upending the usual dynamic of recent years.

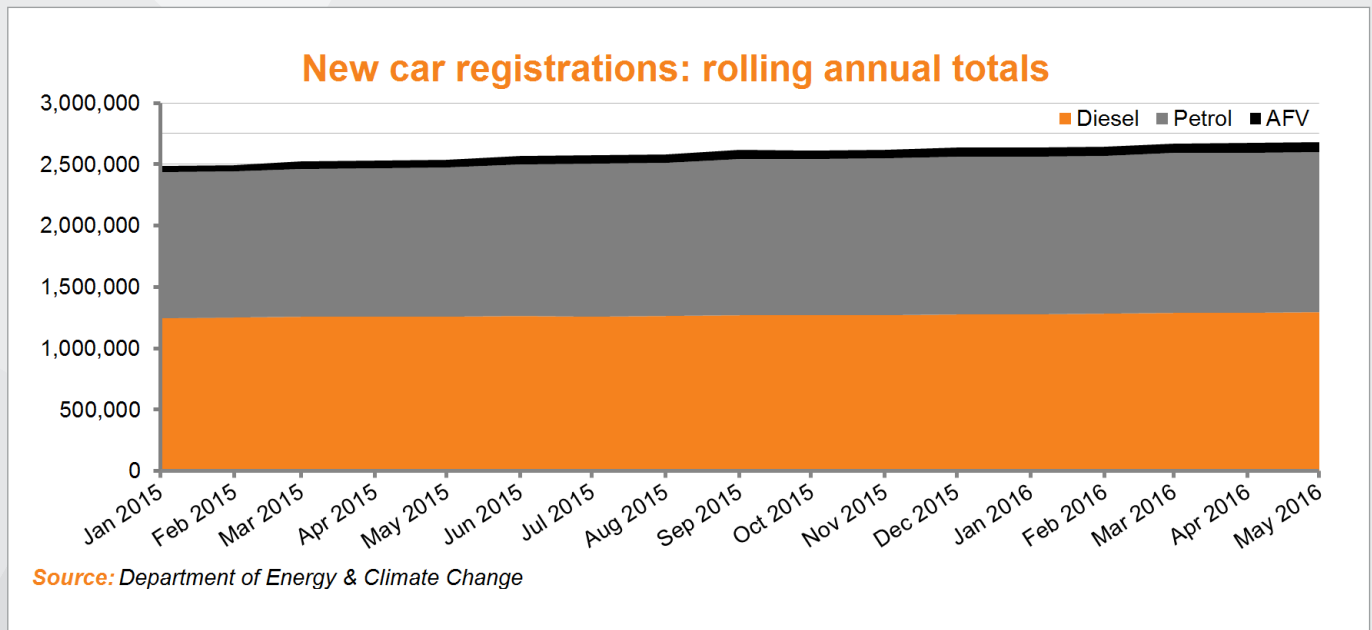
This hasn't been the case since the beginning of March, but the difference between the two fuels is currently so slim as to be negligible.

So far as its comparative pump price is concerned, diesel might seem particularly cost-effective at the moment.

2. The marketplace

(continued)

Registrations of diesel cars



The number of new diesel cars being registered has been quite flat over the past couple of years. In the year to January 2015 there were 1,242,545 registered. In the year to May 2016 the total was 1,294,871. This is growth of just over 4 per cent.

Meanwhile, the number of petrol registrations has risen by 9.6 per cent, whilst the number of alternatively-fuelled registrations has risen by 48.6 per cent, contributing to a reduced market share for diesel cars.

In the year to January 2016, diesels accounted for 50.0 per cent of all cars registered. They now account for 48.3 per cent.

However, the figures for individual months reveal that diesel cars aren't in total decline just yet. 101,922 were registered in May 2016, which is 5 per cent higher than in May 2015.

3. The politics

The Supreme Court

Five years ago, the legal group ClientEarth launched a case against the UK Government for consistently breaching the European Union's limits on NO₂ emissions. This case eventually reached the Supreme Court in 2013.

The Supreme Court's final ruling came in April of last year, and found in favour of ClientEarth. The President of the Court, Lord Neuberger, decreed that 'the Government must prepare and consult on new air quality plans for submission to the European Commission... no later than December 2015'.

The UK Government

In December, the Department for Environment, Food & Rural Affairs (DEFRA) published a report called *Improving air quality in the UK: Tackling nitrogen dioxide in our towns and cities*. This was, in effect, their response to the Supreme Court ruling.

There were several policies within this document, although the most significant was the introduction of Clean Air Zones in several cities. This means that, by 2020, the dirtiest diesel vehicles – which DEFRA describes as 'old polluting buses, coaches, taxis and lorries' – will have to pay to drive through the centres of Birmingham, Leeds, Southampton, Nottingham and Derby. No private cars will be subject to this charge, nor any vehicles that meet the latest emissions standards.

The DEFRA report also extolled the virtues of ultra-low emission fleets. In its words, 'Not only does [this] support growth and UK innovation, it is also the most significant action that can benefit both air quality and reducing carbon emissions.'

Even with this plan, DEFRA still envision that it will take until 2020 for most areas of the UK to be compliant with the EU's NO₂ limits. Or 2025 in the case of Greater London.

Another of the Court's judges, Lord Carnwath, added that the Government 'should be left in no doubt as to the need for immediate action to address this issue'.

As NO₂ is a particular by-product of diesel engines, many commentators believed that this ruling would result in action against diesel vehicles. The Daily Telegraph even reported that 'diesel cars could be phased out in Britain'.

The Government's response to the Supreme Court ruling is summarised below. It has not, however, been sufficient for ClientEarth. In March, they launched a new case in London's High Court.

This delay is a large part of the reason why ClientEarth is continuing its legal action.

DEFRA isn't the only government department to have responded to the Supreme Court ruling. In his Autumn Statement of 2015, the Chancellor of the Exchequer George Osborne revealed that the diesel surcharge – a three percentage-point supplement added to the Benefit In Kind (BIK) rates of diesel company cars – would persist for another five years until 2021. It was originally meant to have expired earlier this year.

Aside from this, however, the Chancellor hasn't yet done as much as many observers might have expected. In his most recent Budget, he announced a review of the current system of CCT, although he confirmed that it would continue to be based on CO₂ emissions, rather than on emissions of NO₂.

But could there be more to come? In a more recent interview, the Transport Secretary Patrick McLoughlin implied that previous governments were wrong to incentivise the purchase of diesel vehicles by focussing on CO₂ ahead of NO₂. 'It is something,' he said, 'the Chancellor will need to look at in due course.'

3. The politics

(continued)

Environment, Food and Rural Affairs Committee

The Parliamentary watchdog that supervises the work of DEFRA – the Environment, Food and Rural Affairs Committee – recently published its own report on air pollution. It agreed with the general principle of Clean Air Zones, although it wants them implemented more extensively and effectively. ‘Charging powers are planned for only the five cities with the worst pollution yet dozens are areas breach EU limits,’ the committee noted. ‘We recommend that DEFRA extends these powers to other councils in its Clean Air Zone legislation so that communities which wish to do so can tackle pollution hot-spots in this way.’

Devolved governments

The Scottish Government has also published a plan for dealing with air pollution, entitled Cleaner air for Scotland: The road to a healthier future. This includes a range of measures, but it rests on two frameworks: the National Modelling Framework, which looks to establish a standard approach for evaluating air quality, and the National Low Emission Framework, by which local authorities can assess their own needs and introduce policies as they see fit.

Meanwhile, the Welsh Government cites a number of policies that it has already introduced, or is set to introduce, to improve air quality. These include a grant scheme, launched in 2012, for local projects aimed at cleaning up urban areas. There are also various transport modernisation programmes in progress, such as the electrification of certain train lines in Wales.

Alongside existing measures, which include the creation of cleaner public transport systems in Belfast, the Department for the Environment for Northern Ireland is also embarking on a review of its clean air policies.

London

London has been the main site of recent action against diesel emissions. Even before the Supreme Court judgement, the capital’s Mayor at the time, Boris Johnson, announced that the city would introduce the world’s first Ultra-Low Emission Zone (ULEZ). From September 2020, under his plan, vehicles travelling through the city centre will have to meet the latest EU emissions standards, or pay a daily fee of between £12.50 and £100 – depending on the vehicle – in addition to the usual Congestion Charge. It is thought that this policy will result in 80 per cent of central London falling within EU limits for NO₂ emissions in 2020.

The London Assembly’s Environment Committee responded to the then Mayor’s plan with its report Driving away from diesel. This endorsed the ULEZ, but called for a ‘faster, wider and stronger’ version of it. This could include, on their account, a charge for all diesel cars – regardless of whether they meet EU standards or not – provided that the national government were to also introduce a scrappage scheme that helps motorists change from diesel to alternative fuels.

This general thinking – strengthening the ULEZ – has been adopted by the new Mayor of London, Sadiq Khan. He has already unveiled proposals to introduce the ULEZ a year earlier (2019) and expand the zone beyond its current boundaries; extending to the North and South Circular by 2020. He wants to introduce a charge of £10 for the most polluting vehicles in the Congestion Charge Zone (in addition to the current charge) and is also consulting on how a diesel scrappage scheme could operate in London.

The European Union

London’s ULEZ is founded on the Euro 6 standards for diesel vehicles – vehicles that don’t comply with those standards will be hit by the extra charge. However, these standards could soon be out-of-date. The EU is currently working on its new Euro 7 regime, which should be introduced before 2021. The intervening period will also see the implementation of new vehicle tests, designed to more accurately record the ‘real world’ emissions of diesel vehicles.

4. Industry organisations

The British Vehicle Rental and Leasing Association

The BVRLA, the trade body for the vehicle rental and leasing sector, has taken a proactive approach to the problem of NO₂ emissions. Indeed, around the time of the Supreme Court's ruling last year, they had already produced a five-point strategy for achieving reductions. Here are those five points in full:

- Help regional authorities to use their newly devolved transport powers by providing a national framework for ultra-low emission zones.
- Adapt the current tax regime to cover NO₂ emissions (incentivising the adoption of new Euro 6 standard for diesel engine emissions, for example), ensuring that any changes are well-signposted and non-retrospective.
- Re-introduce 100 per cent first-year allowances for companies renting or leasing ultra-low emission cars.
- Provide better in-life incentives – for example, freedom from tolls, congestion charges or parking fees – to encourage greater uptake of ultra-low emission vehicles.
- Do more to support car clubs, car sharing and other alternatives to car ownership, and provide more low-emission public transport.

The Society of Motor Manufacturers & Traders

The SMMT welcomes changes to the emissions testing regime so that the results are more reflective of 'real world' driving. Yet they are also keen to emphasise the advances that have already been made in making diesel vehicles cleaner and more efficient.

Their factsheet on the subject refers to DEFRA figures revealing that 'it would take 50 new cars to produce the same amount of pollutant emissions as one vehicle built in 1970'. It continues: 'UK emissions [of nitrogen oxides] have fallen 81 per cent since 1990 – the biggest reduction of any sector.'

The AA and RAC

Many of the AA's remarks about the current diesel situation have been about the policies that were introduced in the past, when NO₂ was less of a concern, and which encouraged the uptake of diesel vehicles. The organisation's president, Edmund King, was quoted in 2014 as saying, 'Some drivers will feel betrayed and misled because they were encouraged to go for the dash for diesel. In the 1990s there was a near hysteria about CO₂, and yet nobody looked at the bigger picture.'

The RAC have also spoken out about this shift from pro-diesel to anti-diesel policies. Responding to Patrick McLoughlin's recent suggestion – cited in the previous section of this document – that taxes might be increased for diesel vehicles, their spokesman observed: 'The present tax system has for many years favoured diesel over petrol vehicles, not least because diesel cars generally emit lower levels of CO₂. Many drivers and businesses have, in good faith, invested in diesel cars for this reason.' Rather than now punishing these drivers and businesses through their tax bills, the RAC advocates schemes such as Clean Air Zones, as well as a 'concerted effort' to both clean up public transport and reduce congestion.

5. Think-tanks and pressure groups

Policy Exchange

In association with King's College London, the centre-right think-tank Policy Exchange has published one of the most detailed reports on the subject of diesel and air pollution, entitled *Up in the air: How to solve London's air quality crisis*. This was actually published in two parts. The first considered the 'moral, legal and economic case for doing more to tackle air pollution'. The second proposed policies for reducing emissions.

Whilst there is too much in *Up in the air* to adequately summarise here, it's worth noting the first part's scepticism towards official forecasts suggesting that London will be within EU limits for NO₂ emissions by 2025: 'current air quality projections should be treated as a best case scenario, and progress may well be slower.'

And the second part recommends, among other policies, that 'the financial incentives that promoted the uptake of diesels in the first place need to be removed and reversed... Changes to Vehicle Excise Duty [VED], Company Car Tax and Capital Allowances are required to reflect the higher [nitrogen oxide] emissions associated with diesels.' Policy Exchange have suggested elsewhere that the extra tax revenues – of about £500 million a year – could go towards funding a diesel scrappage scheme.

These are proposals for London, although they need not be specific to London. Indeed, Policy Exchange observe that 'this report proposes a mix of policies at London, UK and European level.'

The Institute for Fiscal Studies

The IFS, a research group that focuses on the economy and the public finances, hasn't said much – if anything – that is specific to the recent situation with diesel and NO₂ emissions. But they are held in such esteem by politicians and commentators that one of their old reports, *Fuel for thought*, published in conjunction with the RAC Foundation in 2012, could still prove to be influential.

This report proposed an entire shift away from taxing fuel, be it petrol or diesel, and towards taxing congestion. The justification? 'Without action, there is likely to be a long-term erosion of the motoring tax base. Road use, though, is expected to continue to increase. Road pricing not only targets the external costs of motoring more precisely, generating the potential for significant welfare gains, but also provides a more robust revenue source.'

Fuel for Thought also criticised the diesel surcharge – which the Chancellor has recently extended – for its inconsistency with other forms of motoring taxation: 'The oddest part of the structure remains the 3 per cent diesel supplement which is at odds both with the tax treatment of fuel and the VED system, and should be removed.'

Clean Air in London

The thinking of the longstanding campaign group Clean Air in London is encapsulated by the 'manifesto' it published ahead of this year's Mayoral election. Among its recommendations was a more extensive system of emissions-based road charging than is currently planned for the ULEZ, and which would involve 'ban[ning] diesel from the most polluted places,' and 'payments to walkers and cyclists'.

FairFuelUK

The position of FairFuelUK, a group that primarily campaigns for lower fuel duty, was summed up by its spokesman Quentin Willson during a recent radio interview. 'I've got to argue for clean air, here; I can't take completely the driver's position because I've got to be responsible,' he explained. 'But drivers should not be penalised for doing what they thought was the right thing.' Hence why FairFuelUK's campaign objectives for the next four years include both 'an old diesel car scrappage scheme' and 'diesel pricing parity at the pumps'.

6. Sources and further reading

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