IDEAS FOR INVESTMENT

How to generate revenue for sustainable transport in Scotland

November 2024

transform scotland

CONTENTS

FOREWORD

DR KAREN BARRASS, CONVENOR OF THE TRANSFORM SCOTLAND POLICY FORUM:

“The pace and scale required to transform our communities to tackle climate change and provide more cohesive and accessible public transport services requires unprecedented levels of investment and political will. Budgets are increasingly stretched and when times are hard it is easier for the status quo to endure. Yet we need innovation, we need to think outside the box and look to others for inspiration. That’s why we pooled our collective insight into this report to suggest ways in which sustainable transport investment could be prioritised in Scotland to deliver the services that would enable the public to make the switch.

Our hope is that this policy portfolio will be seen as a valuable resource for policymakers, stakeholders, and advocates working towards Scotland’s sustainable transportation future. Any of these measures in isolation would shift the needle and make public transport both more appealing to local people, but also a more effective alternative to private cars. But in combination – and noting that certain measures may better suit urban or rural areas – they have the power to truly transform how people can get around in a cleaner, more equal and more prosperous Scotland. We need to be trying new things and making bold decisions to challenge how things have been done before.

I extend my gratitude to the dedicated individuals who contributed their time and insight to this report and to the policymakers and community leaders who will use these insights to drive positive change.”

EXECUTIVE SUMMARY

The urgent need for investment in Scotland's sustainable transport infrastructure has never been clearer. Achieving ambitious climate targets requires unprecedented levels of investment and political will, which is harder than ever during a time of strained public finances. As traditional revenue streams like fuel duty decline, the status quo is no longer viable. At the same time, transport must compete with other critical sectors, such as health and education, for limited public funds.

This report addresses the dual challenge of meeting climate goals and financial constraints, with proposals for economic instruments that raise funds within the transport sector itself. These measures not only generate revenue but also target the most polluting modes of transport.

With the escalating financial risks of climate breakdown – such as the costs of mitigation and adaptation – aligning taxation with ecological impacts makes strong economic sense. This approach ensures that those who contribute the most to environmental damage bear a fair share of the costs, and help fund the transition to a cleaner, more sustainable network for everyone.

BUDGET GAPS AND CLIMATE CONCERNS

Scotland's transport sector is the largest contributor to greenhouse gas emissions, undermining efforts to achieve the nation's commitment to reach 'net zero' emissions by 2045. Despite the Scottish Government's goal to reduce car travel by 20% by 2030, progress has been slow, and sustainable transport alternatives remain underfunded. Compounding this issue is a projected multi-billion pound shortfall in public finances as the transition to electric vehicles erodes fuel duty revenue.

To address these interconnected challenges, there is an urgent need to develop new revenue streams that can support the expansion and improvement of sustainable transport infrastructure.

THE CASE FOR INVESTMENT

Investment in sustainable transport is a climate imperative and an economic opportunity. It offers a multitude of benefits for:

- **The environment:** Reducing emissions, combating air and noise pollution, and preserving ecosystems.
- **Public health:** Improving air quality and encouraging active travel options like walking and cycling, which promote healthier lifestyles.
- **Economic growth:** Creating jobs in the public transport sector and stimulating economic activity through enhanced connectivity.

ECONOMIC INSTRUMENTS AT OUR DISPOSAL

The report explores a range of innovative financial instruments and tax reforms to raise revenue and stimulate investment in sustainable transport. Key proposals include:

- **Parking charges:** Implementing parking fees and levies that incentivise the use of public transport alternatives.
- **Road user charging:** Developing a Scotland-specific road user charging system for electric vehicles, modelled after Iceland's approach, to manage road usage and generate revenue.

- **Frequent flyer levy:** Replacing Air Passenger Duty with a levy aimed at frequent flyers to reduce aviation emissions and fund sustainable travel initiatives.
- **Local climate bonds:** Introducing regulated debt instruments issued by local authorities to fund sustainable transport projects directly.
- **Sovereign wealth fund:** Establishing a fund sourced from offshore wind revenues to finance long-term transport infrastructure investments.
- **Land value capture:** Utilising the increase in land values driven by new transport infrastructure to finance future projects through collaborative agreements with the private sector.
- **Scottish Government bonds and Financial Transactions:** Leveraging existing devolved powers to issue bonds and provide loan finance for sustainable transport projects.

RECOMMENDATIONS

The report outlines actionable steps for both Scottish Local Authorities and Ministers:

FOR LOCAL AUTHORITIES:

- Implement Workplace Parking Levies (WPL) in cities and high-employment areas.
- Explore partnerships for local climate bonds to fund public transport improvements.
- Collaborate with the private sector on land value capture strategies to finance new transport infrastructure.

FOR SCOTTISH MINISTERS:

- Review and amend existing legislation (e.g., Road Traffic Regulation Act 1984) to enhance local revenue generation capabilities.
- Develop a road user charging scheme tailored for Scotland's needs, particularly with the rise of electric vehicles.
- Establish a sovereign wealth fund using offshore wind revenues to support sustainable transport investments.
- Reform aviation taxes by introducing a Frequent Flyer Levy to reduce emissions and raise funds for sustainable projects.

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INTRODUCTION

INTRODUCTION

WHAT'S THE PROBLEM?

Scotland faces a critical juncture in transport investment with an alarming shortage of public funds. Public services are struggling, and the revenue stream of fuel duty is no longer sustainable as we shift towards electric vehicles, contributing to a £28 billion hole in the annual UK public purse

Amidst these financial troubles, the country is confronting the harsh reality of failing climate targets, with the transport sector the largest contributor to emissions. Scotland's commitment to be net zero by 2045 is firmly planted to its national commitment to cut the kilometres travelled by car by 20% by 2030, yet little progress has been made since 2021 in implementing plans for traffic reduction. Hence the inadequate investment in sustainable transport alternatives puts Scotland's legally binding climate target in severe jeopardy.

To address the twin challenges of a strained public purse and failure on climate, it is imperative to explore revenue-raising measures that not only strengthen Scotland's finances but also facilitate the transition to a sustainable and equitable transport system.

THE CASE FOR INVESTMENT

Investment in sustainable transport is not a luxury but a climate imperative. Beyond emissions reduction, investment brings environmental benefits such as combating air and noise pollution and preserving wildlife. Public health, accessibility and social wellbeing also stand to be improved by better public transport and active travel provision. A boost in funding in the sector would also have economic benefits by acting as a catalyst for job creation, with projections indicating the potential to double the number of jobs in public transport.

A CLOSER LOOK AT SCOTLAND'S TRANSPORT SPENDING

Concerns regarding Scotland's transport budget are only set to grow since public transport provision must be ramped up in line with the Government's climate targets.

In the current year's budget, the Scottish Government allocated £2.5 billion to public transport and £220 million to active travel. However, recent research has found that, in order to meet our climate targets, an additional £1.7 billion of public transport investment per year will be needed by 2035. Investment in bus priority and active travel are already at risk given the Government's decision to suspend its £500m bus fund and its failure to deliver on its promise to allocate £320 million to walking, wheeling and cycling by 2024/25.

These concerns are exacerbated by the lack of a suitable replacement for fuel duty, which generates over £2 billion of tax income in Scotland. This fund will be greatly reduced as we shift to electric cars.

WHAT ARE WE DOING TO HELP?

In this policy portfolio, we explore the nuance of financing sustainable transport in Scotland, adopting a dual focus on (i) raising funds and stabilising public finances and (ii) fostering a fairer, healthier transport system. We review options for alternative tax measures and funding, from parking charges and aviation taxes to climate bonds.

THE TRICKY TERRAIN OF TAXES

Current transport taxes do not adequately account for the negative externalities of road transport and aviation, including greenhouse gas emissions and congestion. These taxes are also not experienced fairly: for example, the lowest income households spend a far higher proportion of their income on taxes like fuel duty compared to their wealthier counterparts.

There is a general reluctance in politics to have conversations about tax reform but the climate crisis demands action. To date, it has been cheaper to pollute and we will start paying the cost with more than money if Scotland refuses to act.

We recommend that the Scottish Government establishes an independent commission to examine options for reforming tax on transport. We emphasise that any tax reforms should be clearly and honestly discussed with the public to ensure acceptance.

OUR PROPOSALS

New taxes and charges are typically controversial. And in an era of conspiracy theorists inflaming public discourse, and with disingenuous 'war on the motorist' rhetoric still being utilised by sections of the mainstream media, governments are necessarily cautious about measures which may increase the cost of transport. So acknowledging this, each of our policy ideas pays particular attention to the equity considerations raised by the tax or levy as well as the feasibility of adoption in Scotland.

In our proposals for effective tax reform, we advocate for measures that:

- Align with Scotland's legally-binding commitment to achieve net zero by 2045
- Target negative social and environmental externalities (i.e. follow the polluter pays principle)
- Avoid disproportionate impacts on low-income households
- Have a clear purpose which is easily communicated and understood
- Adopt a simple collection approach for ease of compliance

The urgency of initiating a public conversation on transport tax reform cannot be overstated. Scotland must proactively update its tax system to meet the demands of a low-carbon economy, fostering a sustainable future for all.

MEASURES AT A GLANCE

Measure	Description	Feasibility	Next steps
Parking charges	Considers the role that parking policy can play in promoting alternative sustainable transport choices. Examples include raising parking rates and providing public transport alternatives, workplace parking levy and removal of parking spaces.	All of the example measures highlighted are feasible in Scotland, but require political will and a careful place-based approach is required when assessing options because not all areas will benefit from/are appropriate for all measures.	- Review RTRA 1984 legislation which limits authorities' ability to make a surplus from on or off-street parking. - Pursue the introduction of Workplace Parking Levies in local transport strategies, especially in cities and large employment areas.
Road user charging	Discusses the limitations of existing motoring taxation and proposes alternative schemes which will generate revenue and reduce traffic – from both ICEs and EVs.	Early evidence of initial projects suggest that the areas into which funds can be invested are broad and could be introduced in Scotland to fund sustainable travel initiatives.	- Design a Scotland-specific road user charging system inspired by Iceland's model. - Assess legal requirements and collaborate with local authorities to develop an equitable, scalable implementation plan.
Frequent flyer levy	Proposes the introduction of a Frequent Flyer Levy in Scotland as a means to both generate funds for investment in sustainable transport and discourage climate-damaging levels of aviation.	Adverse effects of disincentivising air travel should be minimal since a substantial proportion of flights from Scottish airports are domestic and these journeys are the most easily substitutable by other forms of transport.	- Utilise devolved powers over aviation tax to replace Air Passenger Duty (APD) with a frequent flyer levy (FFL) for Scotland.
Local Climate Bonds	Reviews the use of Local Climate Bonds – regulated debt instruments / fixed income securities issued by local authorities to raise money directly from the public.	Early evidence of initial projects suggest that the areas into which funds can be invested are broad and could be introduced in Scotland to fund sustainable travel initiatives.	- Local authorities could explore introducing LCBs and partnership opportunities with public transport companies to allocate revenue raised to sustainable public transport initiatives.
Sovereign wealth fund for sustainable transport	Explores the opportunity of a national contribution to sustainable transport by creating a Scottish sovereign wealth fund derived from the benefits of the offshore wind industry.	Early evidence of initial projects suggest that the areas into which funds can be invested are broad and could be introduced in Scotland to fund sustainable travel initiatives.	- Create a sovereign wealth fund from the revenues of the offshore wind industry and use it to support sustainable transport projects in Scotland.
Land value capture	Highlights how public transport boosts nearby land values and examines land value capture (LVC) mechanisms to recover this increase, highlighting collaborative approaches for financing future transport projects.	Successful examples, such as the Elizabeth Line and Northumberland Line, show that LVC can be a viable funding tool. Successful implementation in Scotland will rely on local conditions, political support, and stakeholder collaboration.	- Explore collaborative land value capture strategies with the private sector to advance the development of public transport infrastructure and associated commercial projects.
Financial Transactions & Scottish Government Bonds	Examines recent policy initiatives that have been facilitated through devolved funding flexibilities and explores potential opportunities for further sustainable transport support.	All of the example measures highlighted are feasible in Scotland, but require political will and a careful place-based approach is required when assessing options because not all areas will benefit from/are appropriate for all measures.	- Use existing powers for Financial Transactions (a capital grant allocation to support private sector investment) to provide loan finance for capital investment in public transport. - Use existing powers for Scottish Government Bonds to put in place an investment fund for sustainable transport infrastructure, working jointly with Local Authorities.

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PARKING CHARGES

PARKING CHARGES

THREE POSITIVE CASE STUDIES FOR RAISING REVENUE FROM PARKING

SUE FLACK

KEY POINTS

- **Parking charges are a potential source of revenue.**
- **Key challenges** include navigating:
  - governance and administration arrangements
  - restrictive legislation (RTRA 1984) that prohibits authorities from deliberately make a surplus from parking charges
- **Good public transport provision is needed** to ensure acceptability of raising/ introducing parking charges
- **Examples of best practice** include Wales' National Parks, Nottingham's Workplace Parking Levy (WPL) and Lambeth's Kerbside Strategy.
- It is **recommended** that the Scottish Government:
  - Reforms legislation to allow authorities to develop parking strategies which allow funds to be raised for sustainable transport
  - Supports local authorities to pursue the introduction of Workplace Parking Levies, focussing on Scottish cities

Parking charges tend to be controversial but are undoubtedly a potential source of revenue for sustainable transport in Scotland.

All parking provision has a cost, to provide and maintain the space, and it can be argued that charging a reasonable fee is economically efficient and fair, if it covers these costs. If parking is free, car users receive the benefit while bus passengers, walkers and cyclists do not. It can be seen as simply a balancing mechanism. Free or cheap parking does not take into account the environmental and social costs of using cars, which are considerable.

Nottingham's Workplace Parking Levy is an example of success. But other types of initiatives can be more difficult to implement as different organisations are responsible for their parking and public transport options. It is even more difficult when some organisations are public and some are privately owned, such as many parking providers and bus companies.

A further problem is that the legislation in the UK is very restrictive about what most public parking revenue can be spent on. For example, the Road Traffic Regulation Act 1984 (RTRA) requires authorities to not plan to make a surplus from on or off-street parking.

If they accidentally make a surplus, this can be spent on transport initiatives that support the authority's stated objectives, but they cannot raise parking charges deliberately to make a surplus to spend on sustainable transport. This can lead to, for example, the cost of parking a car on the street in a Residents' Parking Zone being significantly less than the cost of parking a bike in a council-provided hangar on the same street. This is clearly wrong and a serious limiting factor in developing a co-ordinated parking and sustainable transport strategy.

However, some authorities and organisations have managed to find ways round these legal restrictions or are making use of other legislation. The following three examples show a range of parking-related initiatives that have either proved successful or show great potential.

These examples recognise that car users have become attached to, or dependent on, their cars and that charging measures are often considered unfair, especially for people on low incomes, or who are living in rural areas with little public transport or who need to use cars for personal accessibility reasons. All have their advantages and disadvantages.

CASE STUDY:
SNOWDONIA / ERYRI NATIONAL PARK

Since 2020, Wales' National Park Authority has been developing a co-ordinated parking management initiative to cater for the large numbers of tourists visiting the area. The initiative includes:

- Increased parking charges for the car parks that are most in demand (and closest to Snowdon / Yr Eryri). In 2023, the minimum price was £20 for eight hours.
- An online pre-booking system for parking.
- A parking app which provides real-time information on available car parking spaces.
- Strong enforcement of parking along roads and verges, with a new signing strategy.

At the same time, five new bus services - called Sherpa'r Wyddfa - have been introduced. These link 'gateways' such as car parks, bus stations, rail stations with key local services and tourism destinations. The busiest part of the Sherpa'r Wyddfa network (between Llanberis and Pen-y-pass) is served by up to four buses per hour. A day ticket is £6 for travel on any bus in North Wales (£13 for a family ticket). Active travel routes have also been identified and work has started to improve them.

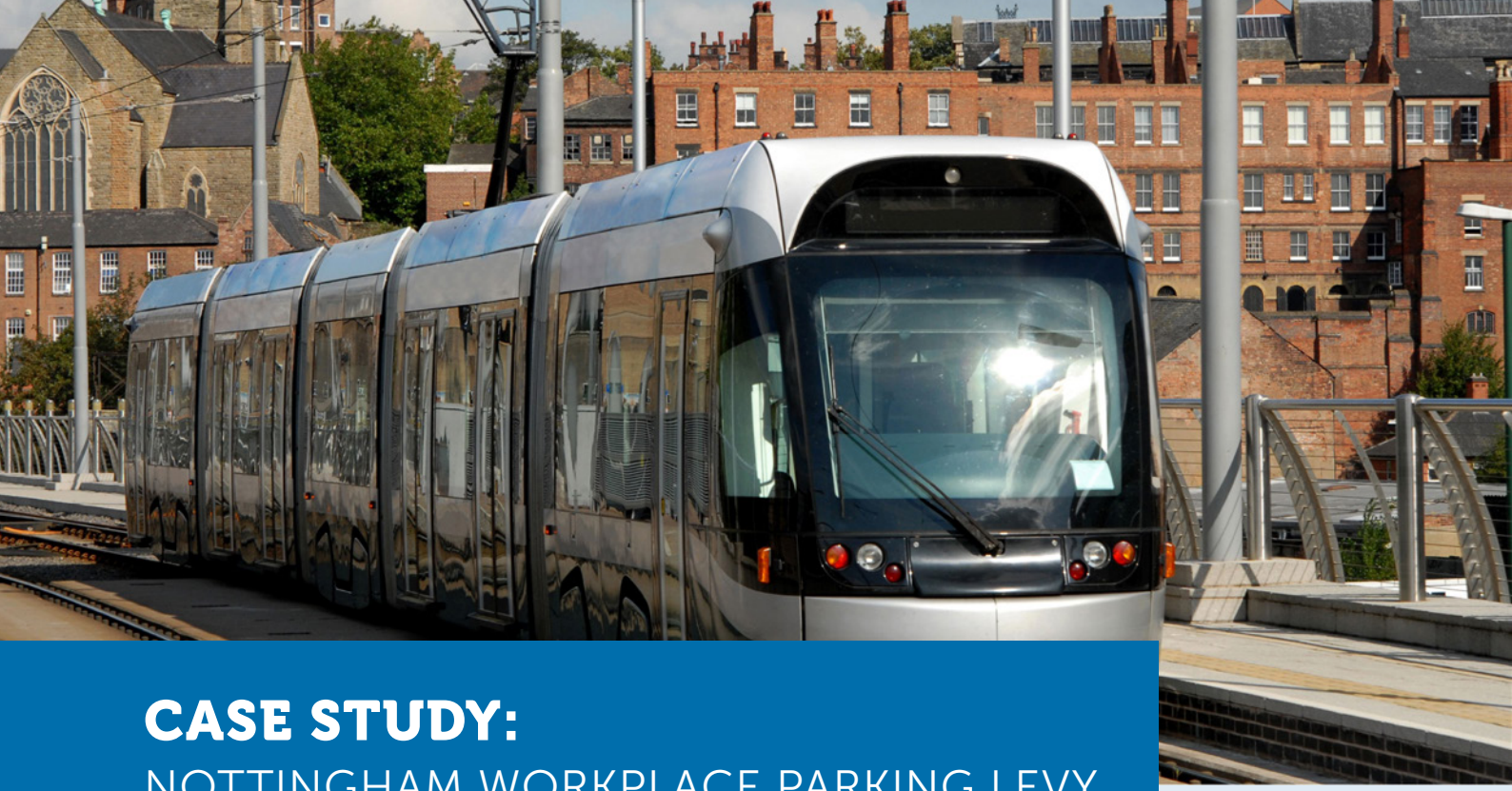
The initiative has been successful. Revenue from parking charges is not used directly for bus subsidies: Transport for Wales has provided subsidies for the buses but they are increasingly becoming commercial propositions. The value of the approach is that it has been developed as a partnership project and includes all transport modes, and it has been widely accepted as a result. It is worth noting that the people paying the higher parking charges are generally visitors to the area, while the local population tends to benefit from better buses and managed parking.

FEASIBILITY OF ADOPTION IN SCOTLAND?

This should be feasible in national parks working in partnership with other relevant agencies.

EQUALITY CONSIDERATIONS

In North Wales, serious attempts have been made to make bus travel affordable for lower-income families, and Scotland would have to follow this example. Although there are free Blue Badge parking spaces available in easily accessible car parks in Snowdonia, there probably should be more, and this is definitely something that Scottish national parks and partners should consider carefully.



CASE STUDY:
NOTTINGHAM WORKPLACE PARKING LEVY

Nottingham City Council introduced a successful WPL scheme in 2012. Employers and educational institutions are charged a modest fee for every occupied workplace parking space, following the England and Wales Transport Act 2000. Revenue raised (between £8m and £10m per year) is spent on specified transport improvements, mainly Nottingham's tram network.

WPL is charged to the employer, not the employee, but it is up to the employer whether they pass a charge on to car commuters. Small employers with 10 or fewer liable parking spaces are given a 100% discount, as the majority of liable parking spaces were found to be with the largest employers. In Nottingham, approximately 50% of the charge is passed on to employees, and the remaining 50% is covered by the employer. Institutions such as hospitals have a 100% discount, as do Blue Badge spaces.

It has been argued that if the employee does not pay the charge, then there is no incentive for car commuters to try alternatives. However, employers are also incentivised to reduce their liability by rationalising and where possible reducing parking, and this also has a mode shift impact. Nottingham has several examples of employers doing this and using excess parking for other more productive uses, such as student housing or teaching space.

A further argument against WPL is that it is self-defeating: if mode shift occurs, then revenues will go down. But this has not happened in Nottingham. Revenue has increased in all years (except during pandemic lockdowns), as when some employees shift to other forms of transport, others tend to take their place, due to economic growth or through latent demand for scarce workplace parking.

Nottingham City Council has developed many legal, digital, and operational procedures related to WPL that have now been proven to work, and the Nottingham scheme is of considerable interest to other cities. However no other WPL schemes have yet been developed to the implementation stage. Most recently Leicester's council decided not to proceed in the context of the current national cost-of-living crisis.

Nottingham did have advantages when WPL was being considered: it already had relatively good bus services and Line 1 of the

tram network was up and running, to general approval. But only a WPL (or other local charging scheme) would provide enough local funding to leverage the Government's contribution to create the desired cross-city and suburban tram network. As well as this, the Council had a long history of working closely with major employers, who were already used to the idea of taking some responsibility for their employees' travel through travel plans and similar initiatives. The Council also had a relatively stable political situation with willing political 'champions' of the scheme.

FEASIBILITY OF ADOPTION IN SCOTLAND?

Scotland's enabling legislation for WPL is in the Transport (Scotland) Act 2019 and both Edinburgh and Glasgow have investigated the potential of WPL. However, because of the lack of public transport alternatives, rural areas in general are unlikely to be considered suitable for WPL, although individual large employment sites in rural areas could have potential.

EQUALITY IMPLICATIONS

A key objection to WPL is that public transport improvements should be provided before any charging scheme starts. This probably means that any WPL scheme will only succeed in cities where public transport is already considered reasonable, and only relatively small-scale improvements are required prior to the charging scheme starting. Nottingham showed how the scheme could successfully take account of some other equality considerations e.g. Blue Badge holders are given a 100% discount.

CASE STUDY:
LAMBETH KERBSIDE STRATEGY

A new approach is being pioneered by Lambeth Borough Council in London. It has focused on converting 25% of the borough's kerbside to non-car parking uses. This does not contravene the RTRA as it does not increase revenue, but it does decrease the availability of scarce kerb space for cars, so it reduces the implicit existing car parking subsidy. It helps to rebalance the existing situation where 94% of Lambeth kerbside is used for car parking, much of it free or relatively cheap.

The strategy aims to remove parking spaces, using them instead for other priorities:

- Enabling accessible and active travel - *"pavements are for walking and wheeling, for everything else there is the kerbside"*
- Creating places for people - *"from parking space to social space"*
- Increasing resilience to climate change - *"our health and our planet's health need nature to thrive"*
- Reducing traffic and emissions from transport - *"efficient ways of getting around benefit us all"*

Focusing on the kerbside has the benefit of being popular among residents and other stakeholders. The benefits of adding bus lanes, bike parking, parklets, car clubs, street trees and rain gardens are often strongly supported and the reduction in parking spaces can be done gradually and sensitively, with residents' involvement. There are no additional charges so there tend to be fewer issues relating to fairness.

FEASIBILITY OF ADOPTION IN SCOTLAND?

This type of scheme is definitely feasible, but it needs to be bespoke to different areas, and may be more difficult to justify in rural and suburban areas.

EQUALITY IMPLICATIONS

It does not involve charging so there are no affordability issues for low-income residents. The action plan can consider specific needs of disabled residents. Allocation of resources for improvements can be done according to an agreed strategy drawn up with community involvement.

PARKING CHARGES ARE THE WAY FORWARD

Parking is a neglected area in transport planning and very few local authorities or other organisations have thorough and well-researched parking strategies covering behaviour change, availability and pricing. Partly this is because parking is such a difficult subject to tackle politically, as every car user has been led to believe they have the right to use almost any public space for parking, without payment in many cases. Changing these attitudes requires political leadership, but it also means that there is a lot of scope for innovation and progressive thinking.

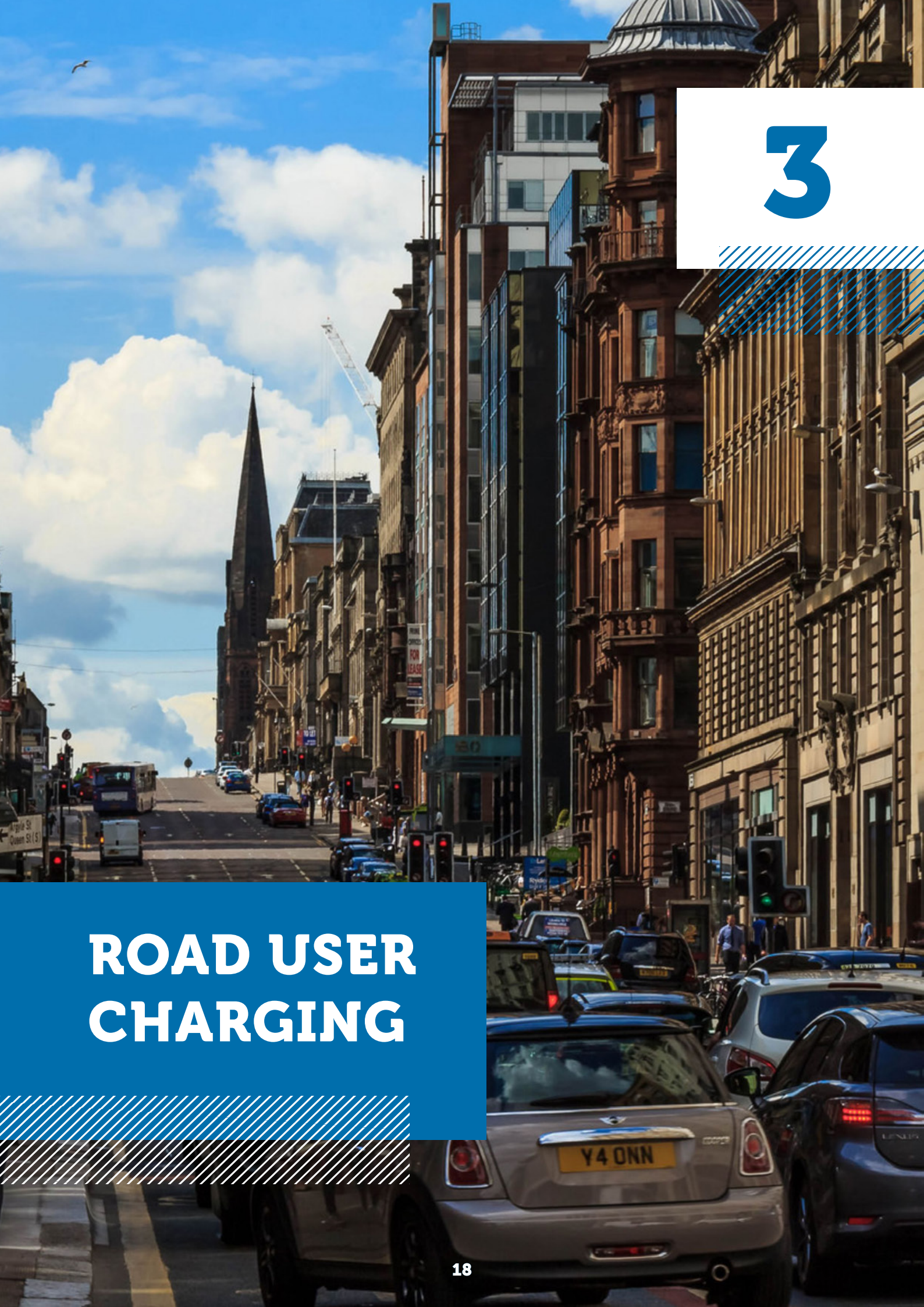
Some international examples have demonstrated what can be done. For example, in Barcelona parking charges pay for the public bike hiring scheme called Bicing, which has been hugely successful, used over 16m times in 2022. There are many examples of Parking Benefit Districts in the US, where parking revenues are reinvested in local areas according to local priorities.

However, this relatively positive picture is partly offset by difficulties caused by the cost-of-living crisis and the current political and populist reactions to clean air and traffic reduction initiatives such as the London Ultra Low Emission Zone. This might mean that promoting parking charges as revenue for sustainable transport may lead to a patchwork of different initiatives across Scotland, depending on local circumstances and governance.

RECOMMENDATIONS

At present the RTRA 1984 limits what public parking revenue can be spent on. Transport Scotland must review this legislation so that authorities can develop comprehensive parking strategies within local transport strategies. This will also allow on- and off-street parking revenues to fund any transport scheme or initiative that is included and properly justified in an approved transport plan.

A Workplace Parking Levy has considerable potential in Scotland, mainly in cities, but it could also apply in large employment areas. Like any change, there are challenges in presenting the proposals and the associated costs and benefits, but a WPL could and should be considered by ambitious and innovative local authorities. The Scottish Government must support and encourage local authorities to consider WPL schemes in their transport plans.



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ROAD USER CHARGING

ROAD USER CHARGING

A NEW IMPETUS BEHIND ROAD PRICING?

COLIN HOWDEN WITH LAURA HYDE-WHITE

KEY POINTS

- Road user **charging charges drivers based on usage** to manage traffic and reduce emissions and other negative externalities.
- **Traditional fuel tax revenues (fuel duty) are declining** as electric vehicle (EV) adoption grows, risking funding for road maintenance and public services.
- **Successful examples** of road pricing exist in cities like London, Stockholm, and Singapore. Iceland has implemented a national mileage-based model which specifically addresses revenue loss from EVs by charging drivers per mile traveled.
- Road user charging can be **more equitable** than fuel taxes, as it charges based on actual road usage rather than fuel consumption.
- **Public support for replacing fuel taxes with road pricing is growing,** especially when tied to investments in public transport.
- **It is recommended that the Scottish Government:**
  - **Design an equivalent of the Icelandic EV charging scheme** for potential UK-wide implementation
  - **Investigate the legislation needed** to implement this as a Scotland-only scheme if UK motoring tax reform is delayed

The reform of transport taxation to place the 'polluter pays principle' at its core has for decades now been the cherished ambition of sustainable transport advocates. Road pricing has long been held as the means in which this could most effectively be accomplished. However, implementation on the ground has been rare and limited, with public acceptability often low, and political leadership generally scarce.

Successful examples of road pricing (also known as 'road user charging') do exist. London's congestion charge remains the pre-eminent example, alongside similar city-based schemes in Gothenburg, Stockholm, Milan and Singapore. But this modest list demonstrates the relative paucity of cities that have taken action, and the general failure of national governments to implement country-wide pricing much beyond a few schemes for trunk road tolling for heavy goods vehicles – with one recent, notable example in the form of Iceland (see below). And while there has been **a demonstrable lack of progress in making the case for road pricing based upon the altruistic aim of congestion alleviation,** there has been even less success in selling the concept around the even more elevated concept of emissions reduction, let alone the Holy Grail of the internalisation of negative economic externalities!

But this gloomy outlook is leavened by the more recent realisation that the transition from Internal Combustion Engine Vehicles (i.e. petrol/diesel cars) to Electric Vehicles (i.e. electric cars) will empty national treasuries due to the latter being reliant on electricity, which is much cheaper, and, crucially, much less taxed than the fossil fuels that continue to power most of the country's car fleet. In the UK, this will mean that the **annual revenues flowing to HM Treasury of c. £35 billion per annum will dwindle and, eventually, fall to zero as ICE vehicles leave the fleet and EVs become the norm.**

Westminster's transport committee eloquently summarised the repercussions of this forecast when it concluded in its 2022 inquiry report on road pricing that

> **"In addition to generating taxation to fund essential public services, motoring taxation plays a key role in managing congestion by regulating demand to use public roads. If the Government fail radically to reform motoring taxation, the UK faces an under-resourced and congested future."**

So while decongesting roads, cutting pollution or delivering an efficient economy have failed to drive change, a more base instinct – *in short, cold hard cash* – is at least beginning to focus minds.

CASE STUDY:
ICELAND: OUR ROADS TO THE FUTURE

Iceland is pioneering a practical solution to counterbalance the loss in tax revenue as a result of the shift toward electric vehicles (EVs).

Currently, 60% of new car registrations in Iceland are electric and this transition away from traditional internal combustion engine (ICE) vehicles poses **a significant threat to fuel tax income.**

To address this, Iceland has introduced a straightforward, distance-based road usage fee – an innovative approach that could serve as a model for other nations facing similar challenges.

The Icelandic road user charge is designed specifically to offset the revenue gap caused by declining fuel duties as EV adoption grows. Under the new system, electric car drivers pay a small fee of 6 Icelandic Krona per kilometre driven (just under 5p per mile).

This **distance-based fee** is simple in design and relatively easy for drivers to comply with. Vehicle owners register on an official website, and their fees are calculated and billed monthly based on mileage. This ensures EV users hold financial responsibility for road maintenance as well as drivers of traditional fuel-powered vehicles.

Several features make Iceland's approach effective:

- It **targets the current EV-driving population**, a demographic expected to expand rapidly as Iceland advances toward a fully electric vehicle fleet.
- The system is **scalable and adaptable**; as the proportion of EVs on Icelandic roads continues to rise, the fee structure can be adjusted to maintain consistent funding.
- The approach is **straightforward** – avoiding the complex restructuring of tax systems.
- It **minimises political resistance** as the system does not impose additional burdens on ICE vehicles in its early stage.

Iceland's approach to road user charging offers valuable insights for Scotland as it moves toward its commitment to 100% of new car registrations being EVs by 2030. Iceland's model, which ties road funding to vehicle *mileage* rather than *fuel* taxes, demonstrates a scalable and adaptable solution that could help Scotland address gaps in its transport budget as EV adoption accelerates.

Adopting a similar model could support Scotland's ambitious targets by ensuring a stable revenue stream for road maintenance and investment in sustainable transport alternatives.

A mileage-based approach is equitable since all drivers contribute to infrastructure upkeep according to their usage. With Scotland aiming for a net-zero transport system and a rapid transition to EVs, implementing an Iceland-inspired road user charge could fill fiscal gaps effectively and support long-term sustainability in the Scottish Government's finances, whilst better reflecting the impacts of disincentivising car use.

THE PROS AND CONS OF ROAD PRICING

In November 2022, Edinburgh Napier University published research, commissioned by Transform Scotland, which identified which measures have been utilised outwith Scotland to manage road traffic travel demand. The report provides a detailed analysis of a number of schemes, plus an extensive bibliography.

With no observable political progress in the intervening two years, the report provides a thorough and contemporary commentary of policy options for traffic demand management. But we will reproduce here in full two summary tables from the report.

CONGESTION CHARGING – KEY POINTS

- ⊕ **Universal reduction in traffic** of between 12 – 33%
- ⊕ Can be seen as beneficial and **supported by business** – particularly where scheme benefits such as transport and environmental benefits can be demonstrated
- ⊕ **Improvement in delivery times** within zone
- ⊕ **Reduced delay** to **high value trips** within zone
- ⊕ **Improved local environment** and opportunity for **better use of space**
- ⊕ Increases in **public transport patronage** and **active travel**
- ⊖ **Effect on retail** difficult to quantify accurately
- ⊖ **Failure to minimise operating costs** of the congestion charging scheme itself can result in limited funds for transport improvements, limiting potential secondary benefits
- ⊖ **Success at pre-implementation referenda** challenging – but may improve in time

NATIONAL ROAD USER CHARGING – KEY POINTS

- ⊕ A national road user charging system is likely to be **urgently required** to replace vehicle excise duty/fuel duty in conjunction with vehicle electrification, **irrespective of any traffic reduction targets**.
- ⊕ Traffic reductions resulting from road user charging are likely to vary by road type and the urban/rural mix, with **reductions of up to 10% possible**
- ⊕ **Business benefits** from road user charging can include more **efficient fleet usage** and **greater uptake of local shopping**
- ⊕ A telematic based road user charging system could **maximise the economic efficiency** of the road network, through **reactive congestion-based time and location charging**
- ⊖ If charges are implemented on certain road types only (e.g. motorways), **true reductions in traffic may not materialise** where local free-of-charge alternative routes exist.
- ⊖ **Public acceptance** of road user charging is low and traditionally has been highly sensitive when changes are made (e.g. fuel duty protests)
- ⊖ **Equity issues** are likely to be raised in association with road user charging in rural areas where public services are more sparse and public transport provision is low

The critical benefit of the road pricing approach is its traffic reduction potential, with a range of 10% to 33% seen as possible (contingent on scheme design). In the context of the Scottish Government's commitment to reduce traffic levels by 20% **no other single transport intervention has the potential to deliver this level of transformational change.**

EQUITY IMPLICATIONS

Road pricing schemes will vary in their distributional impacts according to specific scheme design, and so it is difficult to make sweeping generalisations about likely impacts. However, some impacts would be generally expected to result. For example, **local road pricing schemes which reduce traffic levels should be expected to have an unambiguously beneficial impact for non-car owners** (e.g. bus users, pedestrians and cyclists). And as non-car ownership skews towards women, young people, and those on lower incomes, the **general distributional impacts will tend to be substantially progressive in impact.**

Urban/rural impacts need to be considered. The 2022 Napier report concludes that "rural areas are unlikely to be the best place to target for many reasons", citing factors such as low public acceptance, impracticality, limited public transport alternatives and

potential diversion of business to other areas. So city-based road pricing schemes can be expected to have no direct impact on rural areas. Indeed, a shift from national fuel and vehicle taxation to city-based road pricing would be expected to reduce the relative tax burden for rural dwellers. However, it would be expected that locally-raised revenue would be re-invested locally, so **consideration would have to be given to how investment levels could be maintained in rural areas.**

Transform policy forum member Hussein Patwa has noted that

> **"taxis are a common mode of transport for many people who need to travel within or outside the congested area, especially for those who have limited mobility, disability, or special needs", and that road pricing "may have different equity implications for those who require using taxis out of necessity, depending on the design and implementation of the policy."**

Taxis are exempt in the London congestion charge scheme, and were due to be exempt in the failed Edinburgh scheme. Hussein noted that road pricing "may make taxi travel more convenient and attractive for those who need it, as they may face shorter waiting times and faster journeys"; however, he raises the prospect that it could conceivably "create an incentive for taxi drivers to increase their prices to take advantage of the reduced traffic and higher demand".

PUBLIC ACCEPTABILITY BECOMING MORE FAVOURABLE

The House of Commons Transport Committee could not have been more blunt in its assessment when it said that

> **"the history of road pricing is a history of public unpopularity. Fifteen years ago, for example, a petition against the introduction of road pricing attracted more than one million signatures. As a result, road pricing has acquired the reputation as a policy that is too unpopular to implement."**

However, the Committee's view was perhaps rather too bleak, and, indeed, maybe rather outdated in its outlook. The Green Alliance reported in 2021 that **59% of people support reforming the tax system** to make environmentally damaging behaviour more expensive with one 12% opposing. In its 'Miles Ahead' report (2022), the Social Market Foundation reported results of polling which found **38% support for road pricing** (with 26% opposed).

Meanwhile, in separate polling, the Campaign for Better Transport found 60% of respondents believed the current system of vehicle taxation needed reform (with 6% opposed), and that **49% supported moving to road pricing** (with 18% opposed).

Our own 'Tackling Traffic' report (2022) reviewed business rather than public attitudes; key themes for this were: the need for business engagement, the reinvestment of revenues raised back into public transport, assessment of impacts, and targeting the right journeys. This was reinforced in the accompanying Edinburgh Napier University research which concluded that hypothecation of revenue and clear objectives are critical to public and business community acceptance of any schemes.

BUT POLITICAL LEADERSHIP REMAINS ABSENT

In his foreword to the Social Market Foundation report, the Conservative peer Lord Young bemoaned the lack of leadership, lamenting that

> **"In 1996, when I was Secretary of State for Transport, I published a White Paper that began to grapple with the need for a better way of distributing the costs of driving, by levying charges according to miles driven. It is just a little disappointing that so little progress has been made in the last 26 years. Much of that, I am afraid to say, comes down to political caution and even timidity."**

Despite the urgings of the House of Commons transport committee, and the vast evidence base available to it, it was indeed "just a little disappointing" that **– 28 years on – the incoming Labour government, in command of a vast majority at Westminster, failed dismally to bring about a more progressive approach in its October 2024 Budget.** It contained precisely nothing on the reform of motoring taxation, instead retaining the previous Conservative administration's decade-long fuel duty freeze. The Economist was withering its assessment that:

> **"Now would have been a perfect time to revisit road taxes. Electric vehicles are spreading quickly and are not covered by fuel duties. Far easier to start taxing them now, before a vocal lobby of EV owners is in place to complain. But [the Chancellor of the Exchequer] did nothing there and, worse yet, continued her Tory predecessors' cowardly habit of freezing fuel duty."**

Where this leaves the Scottish Government's putative 'Four Nations Approach' in support of its own ambitions for its 20% traffic reduction target is entirely moot. But the holes in HM Treasury budgets will increase, and worsen, every year as the transition to an electric vehicle fleet continues, and even if the new Labour administration at Westminster continues to ignore its environmental responsibilities, the fiscal ones will become ever clearer, year after year.

SO WHERE NEXT FOR THE ROAD PRICING AGENDA IN SCOTLAND?

The Scottish Government has correctly come round to the view that it cannot meet its climate targets without reducing road traffic levels, and that we won't see significant levels of traffic reduction until demand management is implemented. But the **Scottish Ministers have so far shirked responsibility for action here**, instead asserting that it is solely the responsibility of Scottish local authorities to deliver such measures, whilst simultaneously failing to provide any financial incentivisation for them to do so. So the Scottish Government's current posture can be seen as at best an exercise in magical thinking.

So our recommendation is that the Scottish Ministers **pro-actively design an equivalent of the Icelandic scheme for charging EV use** that could be implemented across the UK. In parallel to this, it should **investigate what legislation would be required to implement this** as a Scotland-only scheme should UK Labour continue to bury its head

in the sand with regards to the need for the reform of motoring taxation. Surely, after all, a SNP Government at Holyrood shouldn't be seen to be reliant on a Labour Government at Westminster before taking decisive, independent action?

4

FREQUENT FLYER LEVY

FREQUENT FLYER LEVY

FLYING IS THE MOST CARBON-INTENSIVE MODE OF TRANSPORT – AND IT IS UNDERTAXED

LAURA HYDE-WHITE

KEY POINTS

- Flying is the **most carbon-intensive** mode of transport and remains **very unequal** – the richest 10% of travellers are responsible for over 7 times more emissions than those on lower incomes.
- Airlines pay no fuel duty and **air travel is massively undertaxed**, with the UK Treasury losing £5 billion in income each year.
- **Taxing air travel is complicated** due to international agreements and tax powers reserved to the UK.
- However, **devolved powers allow the Scottish Government to tax passengers leaving Scottish airports.**
- Despite available powers, **a new air passenger tax in Scotland is yet to be introduced.**
- A more progressive and fair tax which targets frequent flyers – **a Frequent Flyer Levy (FFL)** – should be considered.
- FFL is both **feasible** under devolved powers and **popular with the public**; only political will is lacking.

Flying is the most carbon-intensive mode of transport. Measures aimed at reducing the number of flights are therefore crucial for tackling the environmental impact of travel. Potential fiscal instruments to disincentivise air travel include Frequent Flyer Levies, aviation fuel taxes, and emissions charges.

Here, we argue for the adoption of a Frequent Flyer Levy in Scotland as a means to both generate funds for investment in sustainable transport and discourage climate-damaging levels of aviation.

THE TAX GAP

In addition to reducing climate emissions, a compelling financial opportunity lies in increasing taxes on aviation. Currently, the sector pays no kerosene taxation and no VAT, meaning that the average car driver pays more fuel duty than airlines. This 'airline tax gap' saw the UK Treasury lose £4.7 billion of income in 2022 – and this is expected to rise to £7.4 billion by 2025.

Research finds that if airlines paid fuel tax at the same rate as motorists, they would be paying £6.7 billion to the UK Treasury each year.

This tax gap will only increase as demand for flights grows, with projections suggesting a 74% increase in passenger numbers by 2050 (compared to 2018 levels). Atn a time when budget constraints are prompting cuts in sustainable transport investment – with communities losing vital bus services, failed commitments to active travel funding and public transport fares rising above inflation – lack of action in addressing this hole in the Government's income is indefensible.

ZERO FUEL DUTY? AN OUTDATED LEGACY

Charging tax on kerosene in the UK, however, is complicated. In an effort to avoid double taxation, the 1944 Chicago Convention prohibited the taxation of aviation fuel for international flights. The Convention was established before the end of the Second World War to promote cooperation and create and preserve friendship and understanding among the nations and peoples of the world.

Although it may in fact be possible to tax kerosene under European governance, little progress has been made as a result of the post-war legacy of the Chicago Convention. It is high time for a new international agreement to recognise and prioritise action on the global climate emergency.

Scottish competence in this area is understandably limited given these **international** conventions, but there are levers available at a **national** level to appropriately tax flying.

It is worth noting that some countries (like the US and the Netherlands) already tax fuel for domestic flights – and this can be done relatively simply within the UK. Given that approximately 40% of flights from Scottish airports are to UK destinations, this is worth taking seriously.

WHAT TAXES ARE CURRENTLY IN PLACE IN SCOTLAND? AN INTRODUCTION TO APD AND ADT

Air Passenger Duty (APD) was introduced as a ticket tax in 1994 by the UK Government, with flights in and out of Scotland within its remit. The Duty was specifically introduced as a revenue-raising tax (as opposed to an environmental tax) to ensure airlines make a fair contribution to public finances. It is one of the only taxes on the country's aviation sector.

APD currently raises substantial funds for the Government – approximately £300 million in Scotland (and £3 billion across the UK) each year.

In 2016, the power to charge tax on passengers leaving Scottish airports was devolved to Scotland, meaning the responsibility for APD now lies with Holyrood. The result of this transfer of power means the Scottish government is free to make its own arrangements with regard to the design and collection of any replacement tax, including consideration of the environmental impact. A Scotland-specific replacement to APD has been proposed as a result: the Air Departure Tax (ADT).

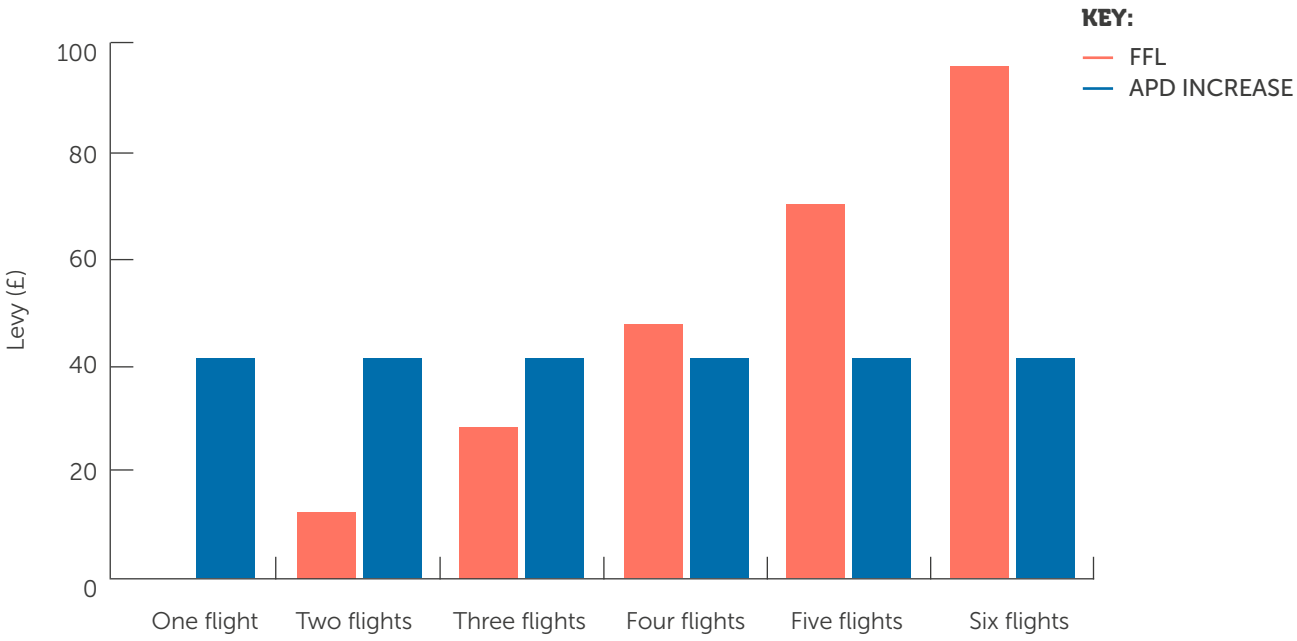
DELAYS TO SCOTTISH POWER OVER TAX

The introduction of ADT was scheduled for 2018 but has been delayed due to unresolved issues regarding exemptions for the Highlands and Islands region. As such, APD remains in place in Scotland. Six years on, no revised date has been set for the introduction of ADT.

The fact that the delays have left Scotland subject to the UK's APD is particularly concerning in light of the UK Government's decision to cut the Duty by 50% in April 2023. This has resulted in a significant drop in income from the aviation sector, as well as introducing an additional competitive disadvantage for Anglo-Scottish rail operators whose routes mirror the Edinburgh-Glasgow and Glasgow-London flight corridors.

PAYING A FAIR SHARE: AN INTRODUCTION TO FREQUENT FLYER LEVIES

A Frequent Flyer Levy (FFL) is often cited as the most progressive alternative to aviation tax, with the tax impact falling disproportionately on high-income groups. The levy would see those who fly the most paying more into the public purse, resembling income tax: those who earn more pay more tax.



Illustrative example comparing the tax individuals would pay with a Frequent Flyer Levy compared to an Air Passenger Duty increase, based on how many flights they take in a year. Source: NEF

The levy would replace the current APD, or any new variant for Scotland (ADT). Raising the latter would be a regressive policy (in comparison to introducing a Frequent Flyer Levy). Whilst an APD or ADT increase would see fewer low-income individuals taking flights, the FFL would result in higher earners reducing their flights proportionately more. Given that 70% of flights are taken by just 15% of people, the levy is designed to both limit aviation emissions (reducing demand) and ensure a more progressive distribution of flights.

IS AVIATION TAX FAIR?

Aviation creates problems for society that aren't entirely paid for by those who fly, including emissions, noise disturbances for people near airports, and congestion both in the air and around airports. To address these issues and the inequalities in our transportation system, aviation taxes are required.

Air travel, one of the most carbon-intensive modes, is mostly used by the wealthiest individuals: in the UK, the richest 10% of travellers produce 7.5 times more flight emissions than those with lower incomes. It's crucial for those who fly to contribute their fair share, otherwise demand for flights exceeds a socially just level. Taxes, in this context, ensure that passengers bear these costs, reducing demand to a level that aligns with societal preferences and increasing overall social welfare.

When considering fairness, the Frequent Flyer Levy has been shown to be the most popular and progressive of available policies. In discouraging people from taking multiple flights (typically the richest 10% of Scottish households) in a 12-month period, this levy would reduce emissions and address a major inequality in our transport system.

IS FFL FEASIBLE IN SCOTLAND?

Adverse effects of disincentivising air travel should be minimal since a substantial proportion of flights from Scottish airports are domestic and these journeys are the most easily substitutable by other forms of transport, such as rail.

There is an appetite for progressive aviation taxation in Scotland. Public support for such policies is strong and Scotland's Climate Assembly has recommended the introduction of a Frequent Flyer Levy. Therefore, given that the Scottish Government has the powers to introduce a FFL, the only barrier to implementation is political will.

Disputes over treatment of the Highlands and Islands (H&I) can stunt progress. There is a need to ensure residents and communities in the region for which air travel provides critical connectivity are not disproportionately disadvantaged by a new tax. The existing (APD) exemption that applies to H&I regions should therefore also apply to a Frequent Flyer Levy. Emissions from the region are small, the need for air connectivity is higher than in those parts of Scotland with better rail connectivity, and these flights are already subject to the Scottish Government's commitment to **zero-carbon flights by 2040**.[1]

A COORDINATED APPROACH

A Frequent Flyer Levy is legally possible at both a national and European level. In fact, there is a strong case for moving towards consistent air ticket taxes across Europe.

Though legally achievable, obstacles to the introduction of a FFL include concerns around GDPR (General Data Protection Regulation), individual identification and price transparency. Recent research shows that these challenges can be overcome, particularly with a pan-European approach. Nevertheless, individual countries can and should be the first step for implementing the FFL. In the long term, the FFL is best implemented alongside complementary measures such as a kerosene tax, distance-based charges, and regulations to cap the number of flights. This is especially important for private jet flights and routes possible to travel by train, for instance.

A UNIQUE OPPORTUNITY IN SCOTLAND

The aviation sector's prolonged under-taxation and over-subsidisation has resulted in artificially low prices for air travel.

Scotland now faces a unique opportunity to take the lead on fairly rebalancing pricing and reshaping its aviation taxation policies; leveraging them as a dual-purpose tool for revenue generation and climate mitigation. By actively supporting the introduction of a Frequent Flyer Levy, Scotland can lead the way in adopting progressive transport taxes which follow the 'polluter pays' principle.

This approach aligns with public sentiment, addresses equity concerns, and contributes significantly to the global fight against climate change while funding essential sustainable transport initiatives – which suffer from chronic underinvestment.

It is clear that the introduction of a FFL to raise money and support investment in climate friendly transport is limited by political will. Both public support and appropriate powers are already secured.

1 Small aircraft and short distances involved make those crucial H&I flights particularly amenable to technological solutions in a way that simply does not apply to the rest of the aviation sector.

5

LOCAL CLIMATE BONDS

LOCAL CLIMATE BONDS

AN OPPORTUNITY FOR LOCAL AUTHORITIES TO RAISE RING-FENCED FUNDS FOR ZERO-CARBON TRANSPORT

DR KAREN BARRASS

KEY POINTS

- Local Climate Bonds (LCBs) are debt instruments issued by local authorities to **raise funds directly from the public**, by crowdfunding or other means, for projects aimed at reducing emissions.
- Several local authorities have issued LCBs since 2020, with **funds ring fenced for decarbonisation initiatives.**
- In Warrington, England, an LCB pilot raised £1 million for projects including a solar farm and support for the transition to electric buses.
- LCBs may **favour investors with disposable income**, raising equity considerations.
- The **use of LCBs in Scotland to fund public transport improvements is feasible**, though using funds to improve affordability of fares may require further assessment and partnerships.

INTRODUCTION

Local Climate Bonds – also known as Council Climate Bonds, Local Green Bonds and Community Municipal Investments – are regulated debt instruments / fixed income securities issued by local authorities to raise money directly from the public.

In partnership with Abundance Investment, eight local authorities[2] have raised £6.4m via LCBs since 2020 to generate funds for a range of projects designed to reduce emissions, including solar panels on schools and council buildings, and electric vehicle charging infrastructure.

For example, since 2020, West Berkshire has installed over 100 electric vehicle charging points as a result of its LCB. Westminster Council raised £1 million from 484 investors in nine days in March 2023.

Through Local Climate Bonds, local authorities can ringfence funding for initiatives specifically designed to decarbonise their area. Almost 2,000 investors have participated in local climate bond investment across all of the projects

2 West Berkshire, Warrington, Westminster, Cotswold, Camden, Telford and Wrekin and Lewisham

initiated to date and the Green Finance Institute estimates that up to £3 billion could be mobilised by local authorities developing their own bonds.

Whilst more research is needed, LCBs can mobilise local residents and institutional investors (such as local authority pension schemes) and enable councils to engage citizens as investors, with a minimum investment of £5 required. Another benefit is LCBs can be less complex for citizens to understand compared to other investment products.

Some local authorities have opted to issue these instruments in the form of peer-to-peer loans (rather than bonds), which allows local authorities to issue instruments that are ISA-eligible, offering a way for investors to earn tax-free returns.

SUCCESS IN WARRINGTON

In May 2020, Warrington, alongside West Berkshire, was one of the first local authorities to announce a pilot scheme for LCBs. Their bond was issued in August 2020 and closed in November 2020. It raised £1m whilst active. More than 500 investors contributed to the bond, with an average overall investment of £1,921. The bond was structured as a five-year investment with a 1.2% return rate. Return payments are made to investors every six months, with the option for these interest payments to be donated back to the council – 11% per cent of Warrington investors did so with their first payment.

Warrington Borough Council has invested in a solar farm and battery storage plan in Cirencester with the investment. It will supply clean energy to the grid and an income revenue for the council. The farm was one of the central elements to Warrington's ZEBRA scheme - to replace its diesel bus fleet with electric buses and supporting infrastructure. All the power at the new bus depot will be purchased from the solar farm. Warrington will receive any surplus income generated from the solar farm to support the delivery of key public services.

The solar farm is held by a 100% council-owned company. According to a case study written by the LGA about the Bond:

> **"[T]o de-risk the investment, the solar assets were created and commissioned by GRIDSERVE prior to transfer of ownership to the council as a working asset. Warrington Borough Council had already pioneered a commercially viable model through the development of two previous solar farms in York and Hull. These farms are already exceeding expectations for their performance and financial returns, showcasing the financial viability of renewable investments."**

EQUITY CONSIDERATIONS

LCBs offer a way for local authorities to access funds that enable them to deliver on their climate commitments. Whilst they are open to all citizens and businesses alike – usually through a crowdfunding platform – they essentially rely on people with disposable income to invest.

There may be people that would like to invest, but don't have any spare capital. So whilst the beneficiaries of the projects are the broadest groupings of society, there is an implication that the ability to invest and receive the return on investment will be reserved for those that can afford it.

UK INFRASTRUCTURE BANK LEADS THE WAY

The UK Infrastructure Bank (UKIB) has £4 billion to lend to local authorities for eligible infrastructure projects. It currently offers up to 50-year loans at gilts + 40bps[3] with a minimum loan size of £5 million. Potential projects must meet UKIB's investment criteria to:

1. Drive regional and local economic growth and / or support tackling climate change
2. Be infrastructure assets or networks in priority sectors including transport; and,
3. Be intended to deliver a positive financial return.

Two of UKIB's advisory pilots were focused on mass transit and zero-emission buses, in West Yorkshire and Greater Manchester respectively. Whilst not specifically targeting affordability as a key objective for support, UKIB states that it is open to working with local authorities to improve access to funding and finance to make public transport more efficient and attractive for passengers, and in this respect warrants mention as a potential source of funding public transport in Scotland too.

FEASIBILITY FOR SCOTLAND

The early evidence from the projects that have gotten off the ground to date suggest that the areas into which funds can be invested are broad.

Given the Warrington and West Berkshire case studies included active travel infrastructure improvements, EV charging infrastructure and public transport upgrades, LCBs hold potential for local authorities in Scotland to improve public transport provision.

LCBs have to date followed a portfolio approach with the beneficiary projects being identified as part of a package. The ownership structure of public transport across Scotland needs consideration too as it may not be possible for those areas where the bus company is independent for public transport to benefit from the establishment of LCBs. Although businesses have been key partners to the projects that have been successful to date, there is potential that a partnership between local authority and bus company could be feasible.

Bonds can be used to boost skills and jobs – these instruments are flexible and can be moulded to specific council objectives – so there is potential to explore.

Authorities may feel they lack the knowledge and experience to launch a similar bond, but the concept is simple and straightforward. The Green Finance Institute issued a set of guidance for local authorities on Community Municipal Investments in November 2023.

Given that councils across Scotland are facing budget gaps on the scale of hundreds of millions of pounds, it is imperative that Scottish local authorities explore the potential for local climate bonds in their area.

3 40bps lower than PWLB in most cases.

6

SOVEREIGN WEALTH FUND

SOVEREIGN WEALTH FUND

IT'S TIME TO ENSURE THAT A FAIRER PROPORTION OF THE BENEFITS FROM THE EXPANSION IN RENEWABLE ENERGY ACCRUE TO THE PEOPLE AND COMMUNITIES OF SCOTLAND

TOM FLANAGAN

KEY POINTS

- A Sovereign Wealth Fund (SWF) is a state-owned pool of money set aside for investment in assets, typically **created from a country's surplus revenues** i.e. from exports of natural resources like oil or minerals.
- Scotland has an **opportunity to create a Sovereign Wealth Fund from the country's renewable energy** given that generation is forecast to grow significantly in the coming years.
- Community benefits from renewable energy could be **used for local public transport and active travel improvements**.
- The **governance framework** to facilitate this is already in place.
- Development of a SWF from offshore wind alone **could generate £300 million** for local communities.

A national contribution to sustainable transport can be achieved by creating a Scottish sovereign wealth fund derived from the benefits of the offshore wind industry.

WHAT IS A SOVEREIGN WEALTH FUND?

A sovereign wealth fund (SWF), sovereign investment fund, or social wealth fund is a state-owned investment fund that invests in real and financial assets such as stocks, bonds, real estate, precious metals, or alternative investments such as private equity or hedge funds.

Most SWFs are funded by revenues from commodity exports or foreign-exchange reserves held by the central bank. In some cases, the SWF is derived from the revenue generated by state-owned assets.

The largest sovereign wealth fund in the world is the Government Pension Fund Global of Norway. Launched as the Government Petroleum Fund in 1990 to manage petroleum revenue, it has since become the largest sovereign wealth fund in the world with over $1 trillion in assets.

The fund is designed to give the government room for manoeuvre in fiscal policy should oil prices drop or the mainland economy contract. It also serves as a tool to manage the financial challenges of an ageing population and an expected drop in petroleum revenue, as well as safeguard and build financial wealth for future generations.

The fund was designed to be invested for the long term, but in a way that made it possible to draw on when required.

As it owns a small slice of most of the world's largest companies, it has the ability to influence how they operate. It aims to promote long-term value creation at the companies and minimise negative effects on the environment and society.

As Scotland decarbonises its energy supply and grows its renewables industry the opportunity now exists to create a sovereign wealth fund from renewable energy.

SCOTLAND'S RENEWABLE ENERGY SUPPLY

Scotland has been exploiting its natural resources for energy production for many years. Scotland's electricity supply today is largely decarbonised with renewable generation in 2022 equivalent to powering all households in Scotland for 3.5 years. Scottish Government analysis shows that renewable electricity could rise to over 140% of Scottish electricity consumption. The Scottish Government's Energy Strategy sets its vision for the future energy system, and has set a target to generate 2GW of locally owned energy by 2030.

SCOTLAND'S OFFSHORE WIND CAPACITY

Scotland's renewable energy supply is set to receive a major boost with the expansion in offshore wind energy. Scotland's marine area has an estimated 25% of Europe's offshore wind and tidal resource and 10% of the wave resource. The Scottish Government is committed to building a globally competitive offshore wind and marine renewables industry to advance the transition to a low-carbon economy while ensuring security of energy supply. This is set out in the National Marine Plan for Scotland. There are also a number of planned development sites for offshore wind and marine renewable energy

COMMUNITY BENEFITS FROM RENEWABLE ENERGY

Community benefits are a renewable industry-led voluntary initiative to support communities – often in the form of funds (financial contributions, investment opportunities, support for local projects). They offer an opportunity for communities to work with renewable energy businesses for long-term local benefits.

In its vision for the future energy system in Scotland, the Scottish Government expects energy developers to offer meaningful

community benefits in line with its Good Practice Principles.

These principles recommend that community benefit packages for onshore wind developments should have a value to the equivalent of at least £5,000 per installed megawatt per annum and be index-linked for the operational lifetime of the project. They also suggest that other onshore technologies, such as solar, should aspire to this level.

It is worth noting that campaigners have made the case that this level of benefit to local communities is just 'loose change' given the value of the onshore wind renewables sector. Analysis from 2022 finds that Scotland's onshore wind farms could together produce electricity valued at over £3.5bn – meanwhile, just over £22m will go to the communities which live nearest these farms in payments to support local initiatives. That is, locals will receive just 0.6% of the value of the electricity produced on their doorstep. Based on electricity prices from the end of 2021, it will take the wind farms just two days to produce electricity worth as much as communities will be paid in a year.

The payments from offshore wind farms have been deemed even more measly. Scotland's six offshore wind farms have paid just £150,000 to nearby communities in the last 12 months. Scotland's offshore wind farms are responsible for only 0.7% of community benefit payments, despite making up nearly 10% of wind energy capacity. Campaigners have argued that the figures added to the "overwhelming evidence" that Scotland's offshore wind has been "exploited not for national benefit, and certainly not for the benefit of coastal communities, but for the benefit of corporations".

SUSTAINABLE TRANSPORT CASE STUDY

A number of sustainable transport projects have been implemented as a result of the community benefits programme, illustrating the potential scope of future projects should further funding be made available. One such example, illustrated in the Appendix, is the Stratherrick & Foyers Community Trust, which has used the funding to refurbish community facilities and improve sustainable transport links, installing electric charging points at each location to make a 20-minute neighbourhood a reality in a rural context.

FOR THE CROWN OR THE COMMUNITY?

The Crown Estate Scotland recently secured £755m in fees from the ScotWind leasing round, massively contributing to potential unprecedented profits for the Sovereign – as opposed to a sovereign wealth fund.

The Crown Estate has generated record profits of almost half a billion pounds from Britain's offshore wind farms, as talks continue over how much of the windfall should be shared with King Charles. The royal property manager made £443m in profits in 2022/23, up by almost £130m from the year before, in large part thanks to payments made by renewable energy companies for the right to access the seabed.

Under current rules, the Crown Estate hands its profits to the Treasury before 25% is returned to the royal household in the form of the sovereign grant, which puts the royal household in line for an annual windfall of almost £90m in 2023. The funding formula is now being reviewed before an expected multi billion-pound deluge of wind power profits for the Crown Estate over the next decade.

In 2023 King Charles asked for the profits from Britain's growing fleet of offshore wind farms to be used for the "wider public good" rather than as extra funding for the monarchy.

CONTRIBUTION TO SUSTAINABLE TRANSPORT

Taking King Charles at his word, it is time to ensure that a fairer proportion of the benefits from the expansion in renewable energy accrue to the people and communities of Scotland.

A sovereign wealth fund could comprise a portion of the sales of leases coupled with revenue from the installed power.

For example, a 2% levy on the option fees (the payments made by a wind energy developer to a landowner in exchange for the exclusive right to develop a wind farm on the landowner's property) could provide an immediate boost of over £15m to support capital investment in sustainable transport.

Moreover, with a total of 28.5GW installed wind energy in operation or planned in the foreseeable future, the Good Practice Principles estimate a potential fund of some £142.5m (assuming £5,000 in community benefits per installed MW).

There is an argument that this community benefit is now considered to be low and so, if doubled to £10,000 per installed MW, the fund could easily generate £285m. This could significantly enhance the budget for rural transport provision in the coming years. Given that wind power installations are more likely to be situated in rural Scotland rather than urban areas, this approach could effectively support sustainable transport in regions currently underserved by traditional public transport.

NO GREAT GOVERNANCE HURDLES

Apart from establishing the financial mechanism to capture the community benefits contribution from offshore wind, there should be no great bureaucratic hurdles. The governance framework is already in place for distributing the community benefits from onshore wind and it is anticipated a similar framework would be adopted for offshore wind. The levy on the Crown Estate for offshore wind would operate on a similar basis to the levy on the private operators of onshore wind farms.

There is even an organisation in place to support community organisations in accessing the funding and applying it to eligible projects: CARES, the Community and Renewable Energy Scheme.

Should the Scottish Government wish to top-slice funding for rural transport provision and community transport schemes, for instance, the governance arrangements are also well established.

A direct link between the benefits of renewable energy and a fund for sustainable transport creates a virtuous circle and makes eminent sense in the struggle to address the climate crisis.

LATEST DEVELOPMENTS

A ScotWind announcement in September 2024 involved the Scottish Government awarding leases to various companies for the development of offshore wind farms in Scotland. This decision is expected to generate significant income from the lease sales, which could amount to around £700 million. The goal is to produce renewable energy, create jobs, and support Scotland's transition to greener energy sources.

In the context of the Sovereign Wealth Fund (SWF) proposal, this announcement highlights the opportunity to invest the profits from these wind farms back into Scotland. By establishing an SWF, Scotland can use the money earned from offshore wind projects to benefit public services, invest in local communities, and secure long-term financial stability for future generations.

7

LAND VALUE CAPTURE

LAND VALUE CAPTURE

CAPTURING LAND VALUE FOR IMPROVED PUBLIC TRANSPORT SERVICES

DAVID GILES

KEY POINTS

- **New public transport infrastructure increases land values** nearby, but landowners often contribute little to the costs.
- The **Edinburgh tram and London's Elizabeth Line** are examples of transport projects which resulted in significant land value uplift.
- The **Government has struggled to capture these value increases** through outdated property taxes and traditional funding methods.
- **Collaborative approaches**, including voluntary contributions and Business Improvement Districts, offer promising alternatives for funding.
- The **E-Rail methodology**, using legally binding Contribution Agreements, has successfully funded projects like the Northumberland Line.

INTRODUCTION

This paper explores how new public transport infrastructure often leads to a significant rise in the value of nearby land. When this development is publicly funded, the landowners who benefit the most typically contribute little or nothing to the project costs.

The concept of **land value capture (LVC)** encompasses various mechanisms aimed at recovering some of this increase in value. This paper delves into historical and modern examples of LVC implementation, discussing the potential for a new collaborative application in Scotland.

NEW INFRASTRUCTURE ENHANCES THE VALUE OF ADJACENT LAND

When the first Edinburgh tram line opened in 2014, house prices along its route rose much faster than elsewhere in the city. In 2022, house prices around the about-to-open Elizabeth Line stations in London had already doubled. A study found that development dependent on the new line would create a potential value uplift of £13

billion in residential values and £215 million in commercial values by 2026. Similar results had been seen from the Jubilee Line Extension.

This is not just a modern phenomenon. In ancient Rome, it was known that the provision of publicly provided aqueducts increased the value of neighbouring land. But it was during the 19th century that railway development demonstrated an extraordinary capability to create growth. New towns such as Barrow and Middlesborough arose where railways transported coal and iron.

In the early 20th century railways began to play an important role in creating space for new housing around cities. In London, the Metropolitan Railway extended out into Middlesex to create 'Metroland'. Unusually among railway companies, the Metropolitan Railway was allowed to sell land acquired for railway use for other purposes, and it received some of the profits from the development. But its main focus was on new passengers, and most of the profits from the new suburban estates went to private landowners and developers.

Similar activity took place in Scotland, especially around Glasgow. For example, the Glasgow and Milngavie Junction Railway was largely conceived as a commuter railway and stimulated a great deal of housing development in and around Bearsden and Milngavie.

GOVERNMENT'S INCREASING ROLE IN INFRASTRUCTURE FINANCING

After the Second World War, the whole character of future infrastructure development was changed by two key pieces of legislation: the Transport Act 1947 made the central (sometimes local) government responsible for its future transport development and the Town and Country Planning (Scotland) Act 1947 required developers to obtain planning permission before they could develop land. The first of these highlighted an issue that was already becoming visible in the inter-war period. Even though new public transport infrastructure enhances the value of adjacent land, **many of those who benefit most from it contribute little or nothing towards its costs.** The second provided a potential solution to this problem.

In theory it ought to be possible to capture some of this value through increased taxes on ordinary economic activity arising from the use of the land. Businesses that grow, or new businesses that arise, as a consequence of new infrastructure will probably generate additional revenue from corporation tax, sales tax or income tax paid by employees. In reality, it is usually difficult to identify these gains and even harder to commit the revenue raised to paying for the infrastructure.

The term **land value capture** embraces a range of mechanisms that aim to recover some of this value from those who benefit. Historically, this has always implied some form of taxation related to the ownership, occupation, transfer or development of land.

LAND VALUE CAPTURE

It ought to be simple to capture some of the increase in the value of **existing residential and commercial property** through ordinary property taxes. In Scotland, both Council Tax and Non-Domestic (Business) Rates are essentially based on property values. If these increase, then the taxes collected will increase.

Unfortunately, Council Tax bands are based on valuations from 1991, so existing residential properties will not reflect the impact of new public transport infrastructure. Newly built residential properties will bring new income, but their residents will require additional services. In contrast, rateable values for business rates are based on an assessment of rental value, and were revalued in 2023, so they should reflect any benefits arising from new public transport infrastructure for both new and existing properties.

Both residential and non-residential property purchases are subject to Land and Buildings Transaction Tax (LBTT, formerly stamp duty), privately owned land and property is subject to Inheritance Tax, and both private individuals and corporations are liable to Capital Gains Tax (though principal private residences are exempt). In practice, these gains are difficult to identify.

Historically attempts to capture land value increases have focused on new or supplementary **hypothecated taxes.**

SUPPLEMENTARY TAXES ON NON-DOMESTIC (BUSINESS) RATES

One third of the costs of the Sydney Harbour Bridge were funded by a 0.2% levy on unimproved land value applied to businesses that benefited from the harbour link in that city. Similar schemes supported the development of the Melbourne City Loop (1980) and the Gold Coast Rapid Transit Light Rail Line (Queensland, 2014).

In London, to fund the development of the Elizabeth Line, a £0.02 supplement was added to the rates of all businesses across the city region with rateable values over £75,000. This required new primary legislation. It will run from 2010 until at least 2038, raises around £225m per annum and supports borrowing of around £3.5bn.

Unfortunately focussing on end values fails to address the huge initial gains made when land is re-zoned for development. The value of land around a new railway station in the green belt can increase by up to a hundred times. And the beneficiaries are the landowners and developers, not the eventual owners of the commercial and residential property.

TAXES ON THE DEVELOPMENT OF LAND

Between 1948 and 1985, there was a series of attempts to introduce specific nationwide (GB) taxes on the profits made by developers. These were all by Labour governments, none lasted more than a few years, and all were overturned by subsequently elected Conservative governments. Their main effect seemed to be to delay development. Developers learnt to wait until a change of government altered the rule.

More recently the focus has been on locally negotiated planning obligations, agreed between developers and planning authorities

in exchange for planning permission. Section 75 agreements can include developer contributions to transport infrastructure, but the difficulties of interfacing planning procedures to complex transport infrastructure development life cycles can make it difficult to introduce them, and it is widely believed that they significantly undervalue land value increases.

In England, the concept of a Community Infrastructure Levy (CIL) was introduced by the Planning Act 2008. This gives councils the power to raise funds from developers in their areas to help deliver new infrastructure using standardised tariffs (much more transparent and easier to operate than negotiated planning obligations). A CIL of between £25 and £80 per square metre was used to provide a further £300m of funding for the Elizabeth Line. But this is the exception rather than the rule: money raised through CIL has been insignificant or very low for most local authorities.

THE FUTURE FOR DEVELOPER CONTRIBUTIONS

There seems to be a growing consensus that Section 75 agreements are not a very suitable way of funding public transport infrastructure development. Recent independent research undertaken for the Scottish Government established that 90% of developer contributions to infrastructure covered 'roads and other transport facilities', but in practice this was focused almost entirely on local infrastructure (road connections and bus stops).

The research established that while there was broad consensus that 'most stakeholders were comfortable with the overall approach to developer contributions and saw it as strongly embedded in the planning system'. This was particularly true of contributions to affordable housing which were seen as being 'well understood and accepted – in part because national and local expectations are clear'.

There was 'general agreement that planning obligations should focus on site-specific mitigation including generated local needs' and a clear consensus that 'planning obligations are not generally an effective means of addressing the cumulative impacts of development, or an appropriate mechanism for securing funding for sub-regional and regional infrastructure requirements'.

A better solution for regional or sub-regional infrastructure might be a **Scottish Community Infrastructure Levy**. This seems to have worked well for the Elizabeth Line, but it is important to realise that most of its planning (and financing) took place before the 2008-9 financial crisis. Whether such an approach would work for Edinburgh trams, in tougher times, in a less prosperous city than London, against residual hostility to infrastructure development is a moot question.

AN OPPORTUNITY FOR A COLLABORATIVE APPROACH TO LAND VALUE CAPTURE

Land value capture has been win-lose between landowners and developers on one side and Government (national and local) on the other. An alternative approach to land value capture might look for synergy between the interests of both parties. Are there ways in which the development of public transport infrastructure and related commercial development can be coordinated in the interests of both parties? This section describes and explores alternative approaches based on collaboration between landowners, developers, planners and transport developers.

HISTORICAL BACKGROUND

Local landowners and business people were usually among the key promoters of, and investors in, new railway lines. They did not do particularly well from dividends, with a few notable exceptions, investment returns were not especially exciting. But many put their money into railways because they could foresee the benefits they would bring to their local communities.

THE ELIZABETH LINE

Likewise, in twenty-first century London many businesses could see the advantage of improved east-west communications across the city. They chose voluntarily to commit to contributions of £100m to support the development of what became known as the Elizabeth Line. Many also wanted to be seen to be contributing. Developers at Canary Wharf and Woolwich contributed £300m in exchange for the right to develop retail, leisure and residential property above the stations, and there was a voluntary contribution of £70m from Heathrow Airport.

The Elizabeth Line also had funding from more traditional sources: there was a supplementary Business Rate and a Community Infrastructure Levy, but the voluntary contributions played an important role in its overall success.

In high-density Asian cities it is quite common to charge property owners **connection fees** to interface their property directly to a rail station (invariably via an above-ground or below-ground walkway connection). To work as a funding mechanism, the connection fee needs to exceed the cost of construction, and be referenced to mutually agreeable value uplift estimates.

BUSINESS IMPROVEMENT DISTRICTS

Another approach that could work for more local infrastructure might build on the work of Business Improvement Districts (BIDs). These are business-led partnerships which are created following a ballot of those businesses liable to pay a levy in order to deliver additional services to local businesses over a defined period (normally five years). They originated in the US and Canada, and are now widespread in the UK.

There is no limit on what projects or services can be provided through a BID. The only requirement is that it should be something that is in addition to services provided by local authorities. Improvements often include extra safety/security, cleaning and environmental measures, but sometimes extend to infrastructure including public wifi in a number of town centres, trader-driven pedestrianisation of some streets and Green Infrastructure.

VOLUNTARY CONTRIBUTION AGREEMENTS (VCAS)

Managing complexity in a large public transport infrastructure project can be challenging. The design and procurement process for the transport scheme and the planning process for any developments along the route must maintain its independence from any VCAs. It is imperative that the independence of the planning process and the procurement process are maintained and adhered to at all stages. The local authority and/or transport agency need to be in control of these processes at all times. Edinburgh based E-Rail has developed a methodology for handling such situations.

E-Rail is commissioned by a public sector body to assess and secure LVC contributions from landowners. Development opportunities within 1km of each new station are evaluated to identify landowners and developers who might benefit from the proposed scheme and the likely level of their contribution assessed (based on their benefits).

Landowners and developers must believe that, without their contribution, the scheme may not happen, so this needs to be done early in the project (before all the details of the transport scheme are finalised). The key to the method is that it is not a tax but a sharing of the increased value of the land due to the new transit facilities. For this reason, the method only works when there is no funding in place, or a significant funding gap.

Once the LVC areas of land have been identified and the uplift in value (subject to planning permission being granted) calculated, formal, legally binding Contribution Agreements (CAs) are created for each of them. These are signed by the landowner, the public sector promoter and E-Rail, and placed on the title of the land in question. Each agreement commits the developer to making the contributions (funds are placed in escrow) once the transport scheme is completed and they have gained planning permission for the proposed development. There are time limits on the completion of the transport scheme and on the duration of the commitment (typically between 5 and 20 years).

THE NORTHUMBERLAND LINE

The E-Rail method works on all fixed transit modes and single stations. It has been successfully used on the new Northumberland Line between Ashington and Newcastle. This offers significant opportunities for development along its route, but has failed to proceed for many years due to funding gaps. Contribution Agreements with 21 landowners are expected to raise 25% of the capital cost of the line, around £40m. This far exceeds funding from S75, CIL, Business Rates, etc.

2014 **Initial assessment of development opportunities**
2017 **Formal negotiations with the first landowner**
2020 **Last of CA signed**
2022 **Construction work starts**
2024 **Expected opening**

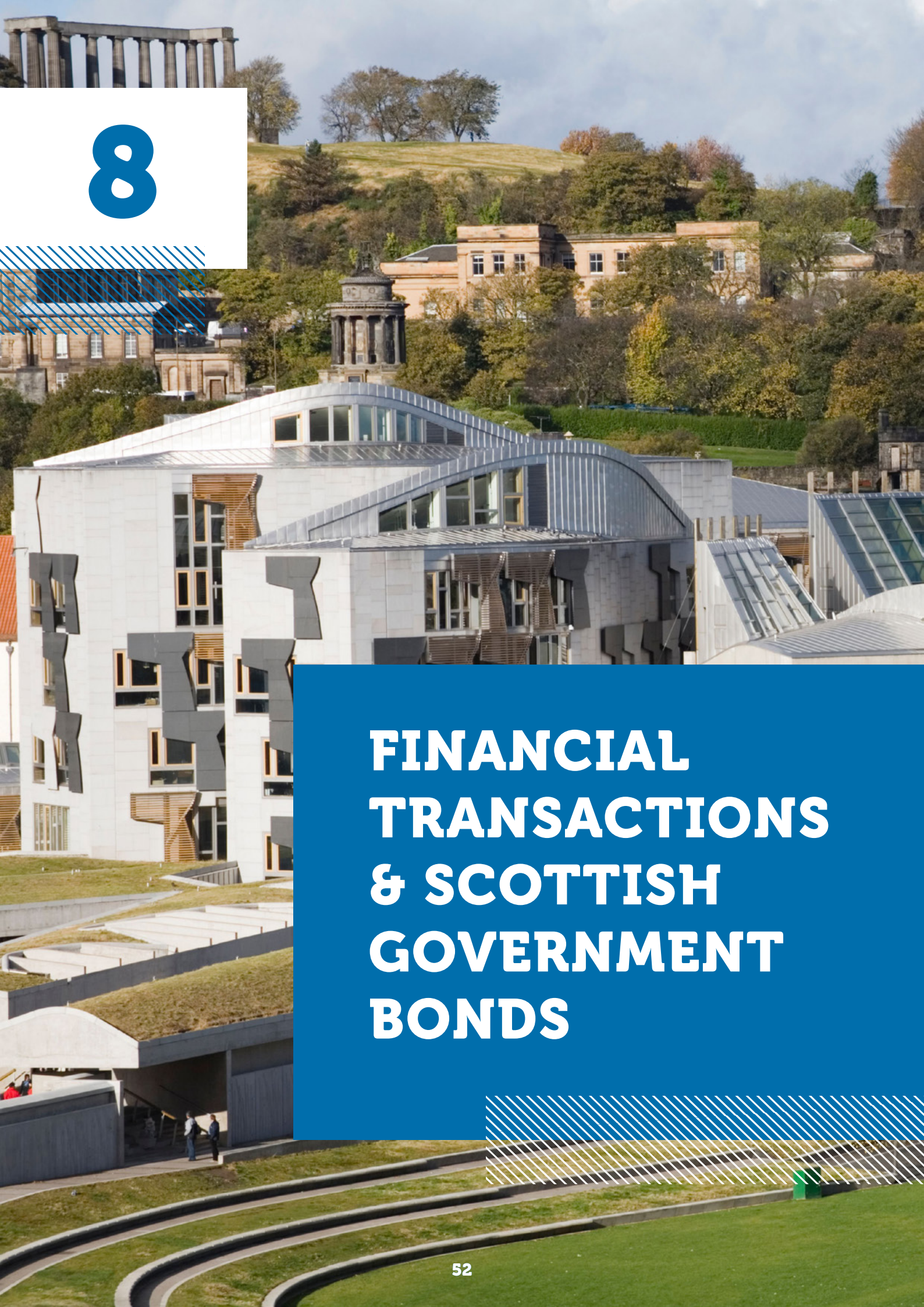
The new line, and three of the new stations, will open in December 2024. The LVC funding was crucial to the delivery of the project given some increased costs. The funds raised from the E-Rail LVC method is not debt, the money does not have to be paid back and can be used for capital or revenue. It must be spent, however, on the specific project associated with the CA.

Northumberland County Council's Strategic Transport Manager believes that understanding the potential economic benefits of reopening the line was vital to the project, and questions whether all six stations could have been funded without this collaborative approach.

"If you can present a case to a developer or landowner that without a contribution the infrastructure will not go ahead, and that the value of their assets will rise if it does, you can really explore the potential. If, for example, a station is built and if through local planning processes a developer gets an opportunity to realise the value of their assets, that uplift in value is shared between the owner and the costs of the infrastructure."

CONCLUSIONS

The success of the Elizabeth Line and Northumberland Line suggest that collaborative approaches may succeed in circumstances where traditional developer contributions may not. Obviously not all locations have the same opportunities as Canary Wharf, but the costs of providing infrastructure are not as great either and the potential funding to be captured is very significant. Business Improvement Districts illustrate the kind of approach that might work for much smaller infrastructure projects.



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FINANCIAL TRANSACTIONS & SCOTTISH GOVERNMENT BONDS

FINANCIAL TRANSACTIONS AND SCOTTISH GOVERNMENT BONDS

THE SCOTLAND GOVERNMENT HAS ROOM TO MANOEUVRE UNDER ITS EXISTING POWERS

TOM FLANAGAN

KEY POINTS

- Scotland has **untapped potential** in using financial instruments like Scottish Government bonds and Financial Transactions to fund sustainable transport.
- The Scottish budget is largely determined by the UK Treasury and the Barnett formula, with some devolved **tax and borrowing powers.**
- There is **flexibility in transport spending**: devolved powers have enabled the likes of the free bus travel for under-22s scheme.
- Despite constraints, the Scottish Government can and should **leverage flexible funding and political will to boost investment investment in sustainable transport.**

Innovative finance is required to fund public transport and active travel in Scotland. But so far, Scottish Government bonds and Financial Transactions remain a relatively untapped area.

We need a shift in mindset to move towards these new instruments in the transport space, we need political will, and we also need to understand how the UK budget works and Scotland's flexibility within that.

This section outlines the baseline assumptions for the devolved Scottish Budget, the flexibilities introduced for more local control over the budget in recent years, how those flexibilities have been used to support sustainable transport and the innovative mechanisms for funding that are still available to explore within the existing framework.

A MARRIAGE OF CONVENIENCE

The Scottish Consolidated Budget comprises a marriage between Departmental Expenditure Limits (DEL) and Annual Managed Expenditure (AME). This reflects the ingredients of the overall UK budget and complies with the principles of devolved management:

- **Accountability** – devolved accountability through the Scottish Parliament.
- **Autonomy** – devolved fiscal responsibilities and freedoms.
- **Transparency** – a readily understood system open to scrutiny.

On this basis, the baseline for the Scottish budget was set at the time of devolution and has been adjusted since for various policy commitments by the UK Government.

The basic Block Grant is calculated using the Barnett formula, a mechanism first established in 1978. Essentially, it is a population-based factor that calculates UK Government departmental spending for the devolved nations depending on how many of the functions are delivered on a devolved basis (the Comparability Factor). The Block Grant is paid for from taxes and revenues collected across the whole of the UK.

In simple terms, the formula can be expressed as follows:

Block Grant =
Change in spending x Comparability Factor x Ratio proportionate population

The Block Grant funding for the Scottish Government currently sits at around £41 billion per annum. However, the Scottish Government can derive income from other sources to supplement its budget, including:

- Financial Transactions
- Non-domestic business rates
- Scottish Income Tax
- Land and Buildings Transaction and Landfill Taxes
- Scotland Reserve and Borrowing
- Other sources (receipts)
- Since 2018-19, more of the Scottish Government DEL expenditure has been classified as AME. This reflects the scale of the Scottish Government's powers to vary the level of self-financed spending.

While adhering to the principles of budget management, the UK Treasury still wields considerable control over the limits of devolved expenditure. HM Treasury sets out the budgeting framework for expenditure control for UK government departments. Its provisions also apply to the devolved administrations, except where bespoke arrangements have been agreed by HM Treasury ministers.

OPPORTUNITY FOR FLEXIBILITY

Within those limits of control, the Scottish Government has been afforded some significant flexibility in recent years, including over elements of transport expenditure.

The Scotland Act 2012, which implemented the recommendations of the Calman Commission, devolved further tax and borrowing powers to the Scottish Parliament. These fiscal powers were enhanced further in the Scotland Act 2016, which implemented the recommendations of the Smith Commission (2014).

For example, the Smith Commission recommended that the power to charge tax on air passengers leaving Scottish airports be devolved to the Scottish Parliament.

Other devolved fiscal powers include the following:

Scottish Income Tax: The Scotland Act 2016 provides the Scottish Parliament with the power to set all Income Tax rates and bands (except the personal allowance, which remains reserved) that apply to Scottish taxpayers' non-savings, non-dividend (NSND) income. A five-band Scottish Income Tax system was implemented for 2018-19 with the introduction of two new bands (a Starter Rate and an Intermediate Rate). HMRC administers Scottish Income Tax as part of the UK-wide Income Tax system and the Scottish Government receives all revenues generated.

Devolved Taxes: From April 2015, stamp duty land tax (SDLT) and landfill tax (LfT) ceased to apply in Scotland and the Scottish Parliament became responsible for the taxation of land / building transactions and disposals to landfill in Scotland. The land and buildings transactions tax (LBTT) and Scottish landfill tax (SLfT) are the replacement taxes. The Scottish Government retains all the revenues generated by these taxes.

DEVOLVED TRANSPORT

The Scottish Government via Transport Scotland has used this flexibility in recent years to promote its policy priorities, most notably in the significant increase in active travel funding which has seen a four-fold increase in walking, wheeling and cycling investment in the past seven years.

Free bus travel for the under-22s was also introduced as a consequence of the Bute House Agreement between the SNP and the Scottish Green Party. The Government committed £359 million in the Scottish Budget to the scheme to provide free bus travel to 2 million people. The policy has been well received, with increased awareness around bus travel and reduced travel costs for young people and their families.

So it is clear that sustainable transport has benefited from flexibilities in the Scottish Budget. Yet, could the Scottish Government go further with the resources and mechanisms at its disposal?

FUNDING FOR INNOVATION

Within the current framework, there remain potential areas of untapped funding that could be applied to innovative and distinctive policy initiatives in Scotland.

One such area is Financial Transactions, which has to be directed towards the private sector. This is an existing capital grant allocation that can be used to support private sector investment. For example, support could be afforded to the match funding required for some City Region Deal projects by academic institutions.

There is no reason why it could not be used to support investment to meet climate change targets in the transport sector. For example, the coach industry, which has a considerable carbon footprint across Scotland, has been bypassed by the Zero Emission Fund. It could be afforded loan finance through Financial Transactions with a shared pay-back scheme.

Another opportunity for investment in innovation is Scottish Government Bonds. Through the framework of the recent Verity House Agreement, a new partnership between the Scottish Government and local authorities, a revolving investment fund for sustainable transport infrastructure could be created.

Scotland has not yet issued any bonds but the option exists to do so, as outlined in the Statement of Funding Policy:

> **"Capital borrowing may be through the Secretary of State for Scotland from the National Loans Fund, by way of a commercial loan (directly from a bank or other lender), or through the Scottish Government issuing their own bonds."**

THE FUTURE OF SUSTAINABLE TRANSPORT INVESTMENT

This brief introduction to the make-up of Scottish Government funding has highlighted some recent policy initiatives that have been facilitated through the devolved funding flexibilities that have been allowed in recent years. It also outlines further opportunities within the current fiscal framework where support might be garnered for further initiatives in sustainable transport.

While at first sight the funding framework for devolved Scottish Government spending seems quite constrained, there are significant opportunities for flexibility and investment opportunities for sustainable transport. It might mean the application of political will and a change in mindset to take advantage of the opportunities on offer.

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ADDITIONAL OPPORTUNITIES

FOR FUNDING SUSTAINABLE TRANSPORT

ADDITIONAL OPPORTUNITIES FOR FUNDING SUSTAINABLE TRANSPORT

In addition to the mechanisms discussed in this essay collection, several other approaches to funding public transport investment have been identified. Although not an exhaustive list, a brief discussion of these approaches is presented below, along with examples and consideration of their feasibility in the Scottish context.

SALES TAX

Sales taxes – imposed by governments on the sale of goods and services – particularly those allocated to transportation purposes, have been implemented in various regions. The United States is a notable example, with many counties or towns having voted for relevant sales taxes in local referenda. Countywide sales taxes for transport purposes are very popular in California and in many other metropolitan areas including Denver, Atlanta, Las Vegas, Minneapolis-St. Paul, and Seattle.

However, in the UK, where sales taxes are managed nationally, the feasibility of such an approach in Scotland appears limited. Unlike the decentralised system in the US, Scotland may therefore face challenges in implementing region-specific sales taxes for transportation projects.

TOURIST TAX

Tourist taxes—additional fees charged to travellers for overnight accommodation—are increasingly seen as a valuable tool for funding local services, including public transport. In Switzerland, for instance, visitors pay between CHF 2 and CHF 7 (£1.81 to £6.34) per night. In Amsterdam, one of Europe's highest tourist tax rates, visitors are charged 12.5% of their accommodation price per night.

The *Visitor Levy (Scotland) Bill* was passed as an Act in July 2024, giving local councils the power to introduce such a levy. Edinburgh is expected to be the first to implement the tax, potentially raising up to £50 million annually. This tax will be particularly effective in tourism-heavy areas such as Edinburgh, the Highlands, and Skye, with revenues earmarked for enhancing local infrastructure and services.

FARE SURCHARGES

Taxes can be imposed on transport users to raise funds for new infrastructure. In essence, these would be supplementary fares. Imposing fare surcharges on specific routes has been a common practice in various regions (often for airports, tunnels and bridges). For instance, Edinburgh Trams charges a single fare to / from Edinburgh Airport at £7.50 compared with a standard fare of £2.00 for all other journeys. The Heathrow Express walk-up fare is £25 compared with £6.70 for the Piccadilly Line.

While this approach may generate revenue for prestige projects, its feasibility more widely in Scotland is questionable. The potential impact on airport workers and travellers raises concerns about equity and practicality, suggesting limited applicability beyond select circumstances.

EMPLOYER TAX

A local employer tax – a levy on businesses to fund public transport – offers a sustainable revenue source. France's 'Versement transport' (VT) is a successful case in which a tax is applied to companies with more than 11 employees, with rates varying with population size, from 0.9% in smaller regions to 2.85% in Paris. The tax funds public transport improvements, enhancing connectivity and property values.

Implementing such a tax in Scotland would require new legislation and administrative systems, as local authorities currently lack this power. While challenging, this approach could significantly support public transport development.

SWITCHING SPENDING FROM ROAD-BUILDING

Redirecting funds from road-building projects towards sustainable transport initiatives represents a proactive step towards prioritising environmental and societal well-being. The Welsh and UK Governments' recent decisions to halt road-building projects in favour of addressing climate concerns serve as pertinent examples.

Given the Scottish Government has devolved control over its transport budget, Scotland could redirect funds away from high-carbon road-building projects towards sustainable transport investment. With several billion pounds allocated for road infrastructure in Scotland, a reallocation could significantly boost public transport and active travel.

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CONCLUSIONS AND RECOMMENDATIONS

CONCLUSIONS AND RECOMMENDATIONS

A STARTING POINT FOR DISCUSSION

Sustainable transport is not receiving the scale of investment necessary to consistently provide compelling alternatives to private car use and flying. This comes at a time when the commercial viability of transport services has been undermined and investment has dwindled due to the calamitous state of the nation's finances.

Innovation in Scottish transport policy-making appears to have ground to a halt. So we're presenting this report as a source of inspiration and as a starting point for discussion. Some of these measures could be implemented forthwith and some will require further thought and perhaps new legislation. But all are worthy of further consideration, and we welcome others to present their own ideas for investment.

RECOMMENDATIONS FOR SCOTTISH LOCAL AUTHORITIES:

- Pursue the introduction of Workplace Parking Levies in local transport strategies, especially in cities and large employment areas.
- Explore introducing Local Climate Bonds and partnership opportunities with public transport companies to allocate revenue raised to sustainable public transport initiatives.
- Explore collaborative approaches on land value capture with the private sector to take forward the development of public transport infrastructure and related commercial development.

RECOMMENDATIONS FOR SCOTTISH MINISTERS:

- Review the Road Traffic Regulation Act 1984 legislation which limits Local Authorities' ability to make a surplus from on- or off-street parking.

- Design an equivalent of the Icelandic scheme for charging EV for road use that could be implemented across the UK; in parallel, investigate what legislation would be required to implement this as a Scotland-only scheme.

- Use existing powers for Financial Transactions (a capital grant allocation to support private sector investment) to provide loan finance for capital investment in public transport.

- Use existing powers for Scottish Government Bonds to put in place an investment fund for sustainable transport infrastructure, working jointly with Local Authorities.

- Explore creating a sovereign wealth fund from the revenues of the offshore wind industry and use it to support sustainable transport projects in Scotland.

- Utilise devolved powers over aviation tax to replace Air Passenger Duty (APD) with a frequent flyer levy (FFL) for Scotland.

- In the absence of action from the UK Government, to establish an independent commission to examine wider options for reforming transport taxation. The urgency of initiating a public conversation on transport tax reform cannot be overstated; however, it will be necessary that proposals for reform be clearly and honestly discussed with the public, and for opposition political parties to engage constructively.

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