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New sources of public climate finance

Discussion paper on global and EU taxes, levies & carbon pricing

Climate Action Network (CAN) Europe is Europe's leading NGO coalition fighting dangerous climate change. With over 185 member organisations active in 38 European countries, representing over 1,700 NGOs and more than 40 million citizens, CAN Europe promotes sustainable climate, energy and development policies throughout Europe.

Introduction

The need for new and additional international public climate finance has been underlined by the Intergovernmental Panel on Climate Change (IPCC) 6th Assessment Report. There are major opportunities to shape bold policy responses in 2023, including through the UNFCCC transitional committee on loss and damage funding arrangements which is tasked to provide recommendations on innovative sources of finance, and the Summit for a New Global Financial Pact in June, with one of four major themes: innovative solutions to provide additional resources in support of countries vulnerable to climate change. Negotiations are also ongoing on the new UNFCCC climate finance goal to support developing countries after 2025, where developed countries should take a lead in contributing and mobilising finance. At the same time alongside debt cancellation by external creditors, climate vulnerable countries can benefit from implementing well-designed new taxes, and accompanying policies and measures, to increase their domestic resource bases.

Climate justice and equity principles should guide the selection, design and implementation of policy options for generating sources of new and additional climate finance. These are necessary for correcting injustices and inequities, but also to increase public acceptance of, and facilitate global political economy towards agreements.

Many climate vulnerable countries have recently championed calls for new forms of revenue generation focusing on polluting industries, debt relief and others. The EU Member States, European Commission and European countries, a number of which supported progress on loss and damage finance through voluntary pledges ahead of COP27, have signalled the need for fossil fuel, aviation and maritime taxation to fund it. By strengthening coalition-building with climate vulnerable countries on these issues and implementing policies domestically they can start to get significantly more public grants-based finance flowing.

Designing effective taxes and levies

Instruments should be designed around the **polluter pays principle**, with objectives to generate revenue but also to dis-incentivise and eventually phaseout harmful activities in line with 1.5 pathways

Instruments should be designed to support **global equity**, embedding or aligned with common but differentiated responsibilities and respective capabilities

Instruments should result in a **net transfer of new and additional finance** that is non debt-generating.

Instruments should be designed with **gender and social justice** in mind and avoid regressive impacts. Any taxation on consumption should primarily target excessive or luxury consumption.

Policy options should deliver new and additional finance at **sufficient scale**.

Considering the need for **adequate and sustainable finance**, an array of permanent and temporary sources should be implemented (since behavioural taxes aim at reducing tax base over time).

As well as international agreements, governments can introduce **ambitious measures at national/regional level**

Reform of the global financial architecture, especially debt architecture and international tax rules, is prerequisite for Global South countries to be able to generate and retain revenue efficiently and fairly. New taxes should be accompanied by **global tax reform**, to help prevent tax avoidance and tax evasion, through a UN-led process for a global tax framework, as recently called for by the UN General Assembly.

Summary key policy options

Key policies which can be designed to support climate justice and equity principles are outlined below, along with implementation options. Table 1 provides a summary of options through scale of financing, estimated date for full implementation, and compliance with the above-mentioned principles. Sources for estimated financial volume are provided in the briefing.

Table 1: Key multilateral policy options for new and additional climate finance revenue, estimated launch and compliance with principles.

| Funding source | Est. revenue/yr | Est. launch | Climate justice & equity |
|--------------------|--------------------|-------------|--------------------------|
| Fossil fuel levy | USD 50–150 billion | unclear | high |
| Air passenger levy | USD 4-150 billion | 2025-2027 | medium-high |
| Maritime levy | USD 40-75 billion | 2025-2027 | high |
| Wealth tax | > USD 295 billion | unclear | high |

Table 2: Key EU-level policy options for new and additional climate finance revenue, proposed share of proceeds and launch

| Funding source | Est. revenue/yr | Proposed share of proceeds | Est. launch | Climate justice & equity |
|------------------------------|-------------------|----------------------------|-------------|--------------------------|
| Windfall profit tax | €7.5 billion | 30% : €2.25 billion | 2023 | low to high |
| Private jet tax | € 325 million | 100% | 2027 | high |
| EU ETS | €24.1 billion | 30% : €7.2 billion | 2025-2027 | high |
| EU CBAM | €1.5 billion | 50% : €0.75 billion | 2026 | low to medium |
| EU financial transaction tax | €34 - 300 billion | 30% : €9 - 90 billion | 2025-2027 | medium |

The remainder of this paper explores these options in more detail.

Exploring key policy options

Fossil fuel taxation

Fossil fuel companies and other highly polluting industries currently benefit from enormous subsidies and lack of mechanisms to account for their negative externalities (implicit subsidies). The urgent need for new taxes, as called for in 2022 by the UN Secretary General, Prime Minister Mia Mottley of Barbados in the Bridgetown Agenda, the EU at COP27, is increasingly recognised, and there exist multiple implementation options including extending windfall profits taxes (explored below), taxing **revenues of extractive fossil fuel companies**, and targeting financial operations of companies to **levy a specific excise tax on dividends or on corporate excise stock buy-backs** (with the US Inflation Reduction Act offering some precedent for this approach, although not limited to fossil fuel companies). The '**climate damages tax**,' long endorsed by civil society, would take the form of a tax or levy on the extraction of fossil fuels (i.e. per barrel of oil, tonne of coal, cubic litre of gas) according to a global rate based on CO₂e. With a universal (and starting from a low base) rate of USD 6 per ton of CO₂, a levy could generate USD 150 billion per year. Revenues would be significantly higher starting at USD 5 per ton, increasing the amount by USD 5 annually until 2030, and increasing the annual rate e.g. by USD 10 (SOP, 2019). To address equity in implementation in different countries, developed countries and rich fossil fuel producing countries could direct 50% of revenue to the loss and

damage fund, and 50% to support the just transition domestically, and in developed countries without or limited extraction, the levy could be applied to refining processes. Lower income countries could make 100% of revenue available for domestic spending. Whilst global implementation is unlikely at this time, parties at the UNFCCC could agree to establish a universal approach to fossil fuel extraction tax, which would then be implemented nationally. A stepwise approach towards this would be opting into a “**solidarity levy**” on a voluntary basis. Fossil fuel companies would voluntarily agree to pay a levy, or a country or group of countries could impose a solidarity tax on companies extracting oil, gas, or coal on their territories, with an agreement to contribute to the loss and damage fund.

EU policy implementation: Given the limited extraction of fossil fuels within the EU relative to globally, EU diplomatic efforts need to be sensitive to and in line with global equity. The EU should take strong action on fossil fuel operations falling within their remit (not just upstream but midstream and downstream, including refining and electricity production). After fossil fuel majors and some state-owned companies made record profits in 2022, temporary **taxes on windfall profits** were coordinated at EU level and implemented at national level via the *Council Regulation on an emergency intervention to address high energy prices*, with revenues largely used to support households hit by high energy prices. To build on this approach **more comprehensive and permanent taxes should be introduced**, applying to all current and future profits over a certain threshold or according to a certain level of excess profits (defined as return to shareholders), provided that at least a minimum percentage of companies’ turnover emanates from fossil fuel related activities.¹ In 2021 the solidarity levy is estimated to have generated EUR 4.4 Bn and in 2022 EUR 7.5Bn (European Parliament, 2023). In CAN Europe’s view the additional mechanism in the Council Regulation for a market revenue cap for inframarginal electricity producers (most often renewables, but also nuclear, lignite) should be excluded, as this mechanism would fail to target the fossil fuel industry specifically. Revenues should primarily be used to support consumers, and a share of proceeds allocated to the UNFCCC loss and damage fund.

Maritime and aviation taxes and levies

International aviation and maritime transport are exposed to major gaps in regulating emissions.

Countries should agree at the **International Maritime Organisation** to implement ambitious mid-term decarbonisation targets and a tax in the form of a **universal mandatory levy, set at an ambitious carbon price according to a ship’s GHG emissions**. A core principle of the IMO is ‘no more favorable treatment’ (NMFT) implying the necessary universality of any economic instrument or target. While CBDR-RC has not gained traction at the IMO, another key principle is the need to avoid ‘disproportionately negative impacts’ (DNI); since countries with different income levels and different maritime dependencies (export/import, tourism etc) will be affected disproportionately by a levy, redistribution of revenues should be key in addressing it. In addition to the necessary steering effect for achieving the Paris climate targets in maritime transport, a levy would generate considerable additional revenue which, in addition to financing the development of a bunkering infrastructure for alternative, low-CO2 emission fuels, could also be used as a new and innovative source of international climate financing. The revenues of

¹ For example, the EU’s solidarity levy is applied to companies who make at least 75% of their turnover in crude petroleum, natural gas, coal and refinery sectors. However, the threshold could be set at a lower level.

a carbon levy of USD 75 per ton of CO₂ in 2030, doubling to USD 150 in 2040, could reach USD 75 billion annually in 2030 and USD 150 billion in 2040 (Parry et al, 2018 in IMF, 2018). At the same time, this levy is predicted to reduce CO₂ emissions from this sector by 15 percent in 2030 and 25 percent in 2040 below business-as-usual levels, while the increase of shipping costs by 0.075 percent of global GDP in 2030 would remain very moderate (ibid.). In 2021, the Marshall Islands and Solomon Islands proposed to the International Maritime Organization (IMO) to impose a volume-based GHG emissions levy on marine fuel that is universal and mandatory (Adamopoulos, 2021). The IMO's Marine Environment Protection Committee in July 2023 (MEPC 80) represents a key opportunity for convergence around climate targets and an economic instrument in the form of a levy, with a coalition of African countries and the EU independently backing such an approach. Use of revenues to support greening shipping and maritime infrastructure, a just transition in most affected countries, and a contribution to the loss and damage fund offer a way forward.

International climate solidarity levies on aviation also offer a way to generate finance, in the form of an air passenger or ticket levy as a surcharge placed on air tickets. While it applies to the air transport service that entails negative externalities to the climate, it is not based on GHG emissions generated by kerosene in a strict sense (IDDRI, 2023). The solidarity levy (or passenger levy) UNITAID on airline tickets has been applied by 11 countries since 2006, including France. Taxing international airfares would be an effective way to apply the polluter pays principle to individuals with high-polluting lifestyles to directly redress those affected by climate-induced loss and damage change. This approach would also effectively cover privileged elites in emerging economies and developing countries, who can afford to take international flights, and whose carbon footprints outstrip those of working-class Europeans. Piketty and Chancel, two French economists, proposed taxing flights with a levy of USD 20 on economy class and USD 196 on business class tickets to raise an estimated USD 150 billion for adaptation in developing countries (Chancel and Piketty, 2015). Other calculations with more moderate levy rates come to lower revenues (IDDRI, 2023). A progressive air travel levy could impose higher payments on business - and first-class tickets, as well as on longer flights. However Small island states in particular, which are heavily dependent on tourism, fear negative economic effects. Exemptions for certain destinations could be explored, or the use of revenues for domestic just transition actions. An even higher level of compliance with equity principles would be via a **Global Frequent Flyer Levy**, however technically implementing this has low feasibility due to difficulty in centralising data on individual ticket purchases to separate companies.

EU-specific policies: in parallel to and dependent on action at the IMO and new aviation taxes, the EU can take additional or complimentary action. The EU is responsible for about one fifth of shipping and aviation emissions of UNFCCC Annex 1 countries. The EU emissions trading system covers aviation and shipping but with insufficiently ambitious mitigation targets and a too limited scope in these sectors, whereas extension of its scope would contribute to climate goals and add an extra \$12.8 billion revenues per year. Transport & Environment recommends extension of the aviation ETS to all departing flights by 2027 and extension of the shipping ETS to all incoming and departing voyages by 2028, and higher green fuel mandates in shipping.

As a stepping stone towards regulating them out of existence, EU member states can tax private jets, super-yachts, expensive SUVs and other **luxury highly emitting transport**, for example through a sales tax or travel-based taxes: a private jet tax based on cumulative flight distances could bring in \$325 million annually (Transport & Environment, 2021).

Financial Transactions Tax

There are several proposals as well as existing forms of **financial transaction taxes (FTTs)** both in the EU and internationally with notable differences and scope. These take the form of a tax on financial transactions, such as the purchase and sale of stocks and derivatives, extended to the most speculative products, although in practice most FTTs now focus on stocks only and sometimes bonds. Under an FTT, a percentage of the asset's value is paid in taxes when it is traded. An FTT, depending on its design, could raise significant amounts, but it is also a speculation prevention mechanism. A global coordinated approach is unlikely at this time, however coordination amongst ambitious implementing countries on scope could support increased and more coherent adoption.

EU-specific implementation: an EU FTT is likely to be part of a proposed package of new own resources this year to address the needs of financing the EU budget and the bonds taken out to fund "Next Generation EU," with a specific proposal of the Commission due by June 2024. Meanwhile, several Member States (Belgium, Finland, France, Ireland, Italy, Poland and Spain) have introduced unilateral FTTs that differ significantly across countries. Such a tool is essential to help bridge the climate investment gaps within the EU, and decision-makers could also decide to assign a portion of revenue directly to international climate finance. Estimates on revenue vary considerably depending on the particular specifications of the FTT proposal examined and also on the assumed effects of the tax on trading volumes. According to the European Commission, the EU-wide FTT as proposed in 2011 could have approximately raised € 57 billion every year from 2014 onwards, with much revenues in additional taxes going directly to member states and an EU own resource contribution offset by reductions in national contributions (European Commission, 2011). By replicating the methodology and tax rate options used by the European Commission's initial study, and scaling it to the current level of financial transactions, CAN Europe estimates that with a flat tax rate of 0.01% levied on both securities and derivatives, revenues could amount to an average of €33.8 billion per year. Similarly, the differentiated model proposed by the Commission, whereby shares and bonds are taxed at a rate of 0.1% and derivative contracts, at a rate of 0.01%, would raise revenues worth €66.1 billion per year, while a flat tax rate of 0.1% on both securities and derivatives could increase the amount to a central estimate of €300.15 billion annually.

Wealth taxes

Systemic and wide-ranging increases in taxation of the super-rich are needed to address worsening global inequalities amidst the recent increases in billionaire wealth (Oxfam, 2023). The **proposals for wealth taxes** that are being discussed are characterised by a **very broad typology**. As possible bases for taxation they take into account, among others, income from commercial operations, from self-employment and dependent employment, from capital assets, rentals and leases; furthermore, tangible assets such as real estate, companies and other types of property; financial assets in the form of savings, securities and shares; and inheritances. Wealth taxes may be imposed on natural and/or legal persons. They are proposed as direct and indirect taxes and their duration could range from a one-off payment to a limited period, or can be conceived as permanent. Furthermore, they are designed as new, additional taxes, as surtaxes on already existing levies or as more progressive taxes. A range of tax options could

be introduced to encompass: **permanently increased taxes on the richest 1 percent, increased capital gains taxes, and increased inheritance, property and land taxes**, as well as **net wealth taxes on the richest 1%**. Potential revenues from wealth taxes are a contentious area as claims would be made on them from all policy fields, but available estimates suggest weighty orders of magnitude. An EU-wide net wealth tax on individuals suggest substantial revenue, yielding additional public income as high as 10.8 percent of EU GDP (using a strongly progressive tax rate), while affecting between 1 percent and 4.8 percent of households and resulting in an effective tax rate of about 0.3 percent of net wealth (Kapeller et al, 2021). Economists and policy experts have called for a “1.5% for 1.5°C” tax on extreme wealth, and a progressive tax starting at 1.5% on individuals with over \$100 million is estimated to raise upwards of \$295 billion (Chancel et al, 2023).

Carbon pricing and carbon markets

Domestic compliance carbon markets that are already in operation offer a ready source of financing for climate action.

EU policy implementation: with recent revisions to the EU’s carbon market system and the introduction of the carbon border adjustment mechanism, the EU and its Member States have clear opportunities to allocate an increased share of proceeds to international climate finance, and to the loss and damage fund.

Under the **EU Emissions Trading System (ETS)**, emission allowances are allocated through auctioning. The revenue generated from this auctioning has grown in the past few years, particularly due to the increasing carbon price. Prior to the recent revision of the ETS Member States (who retain a portion of revenues from their sales of ETS allowances) were only recommended to use at least half of their auctioning revenue for climate action at home or abroad. In 2019, Member States used 67.1% for climate action and between 2013 and 2019 merely 6.2% of ETS revenues for international climate finance contributions (WWF, 2021). New rules now require countries to spend all the revenues generated by the ETS on a transition to a “green economy” and Article 10 (3) of the Directive makes international climate finance in vulnerable third countries a mandatory consideration for Member States when deciding on the use of revenues. Member States failed to agree to a fixed percentage contribution in the revision of the legislation, and the decision is now up to each Member State. Based on revenue generated in 2021, a 15 percent rate would mean approximately € 3.6 billion per year (EEA, no date), and based on an increasing ETS allowance cost, could be much greater in the future.

The **EU Carbon Border Adjustment Mechanism (CBAM)** introduces a price for embedded carbon emissions production of carbon intensive goods imported to the EU, based on a weekly average auction price of the EU ETS allowances. Most revenues are forecast to be used as own resources for the EU budget, and a small portion by Member States. Estimated revenues are €1.5 billion per year from 2026 to 2030 to €2.1 billion by 2030 (European Commission, 2021). CBAM has been criticised by Global South countries due to its potential impacts on sectors, and in effect imposing a tariff on developing countries in order to generate EU income (Germanwatch). Dedicating a share of the revenues to international climate finance including the loss and damage fund could address some of the criticisms, and be seen as a more equitable solution. However, this finance could not be considered to comply with the notion of common but differentiated responsibilities, considering it is finance that has been partly

leveraged from developing countries (while some burden can also fall on importers), and countries affected by CBAM might not be those receiving the finance generated from it. Although revenues are currently designated as EU own resources, a better response to the EU's partner countries is needed and should be explored during the introductory transitional phase ahead of its full operationalisation from 1 January 2026.

Conclusion

Whilst this briefing is not comprehensive, there are clearly a broad menu of implementable policy options at national, EU and multilateral level for addressing climate harmful behaviour and sourcing revenue for international climate finance. The EU should start by moving forward on domestic opportunities: in the quest for new sources of finance for repayments on the recovery package and the next EU budget, a generous share of proceeds should be dedicated to international climate finance. On multilateral policies EU diplomatic efforts need to be sensitive to and in line with global equity, and the EU should engage in active coalition building. Embedding equity and CBDR-RC in policies at EU and multilateral level, and in relevant UNFCCC decisions will help a broader range of countries support their implementation in a multilateral fashion. This should also apply to the loss and damage funding arrangements transitional committee recommendations, which should include principles and guidance on implementation outside UNFCCC.

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