Environmental Taxation In The UK and Scotland
- Changes, Challenges and Landfill Tax
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General Background

1. The principle underlying environmental taxation is that certain activities can have external effects which are undesirable or harmful because of their effect on human health, buildings or habitats and ecosystems, and there is no intrinsic market-based mechanism which effectively discourages or prevents such undesirable or harmful activity, or which will pay for remedying their consequences. The purpose of environmental taxation is therefore to put in place an additional cost factor which is intended to act as an incentive towards changing the market by making the undesirable behaviour relatively more costly and therefore encouraging producers or consumers to change their behaviour. It also helps create room in the marketplace for less harmful alternatives to compete more effectively or to be developed.

2. Examples of taxation in the UK that can be seen as being environmental, or having an environmental component, are the Aggregates Levy, Air Passenger Duty, the Climate Change Levy, Fuel Duty, Landfill Tax, and Vehicle Excise Duty. As well as these national based taxes there can also be local environmental taxes. In the UK an example of this is the London Congestion Charge. In Italy and Australia there have been local taxes on storm water drainage collection systems, known colloquially as Rain Tax (a name also used for certain water charges in England and Wales which were abolished in 2008 following a campaign led by churches, the Scout Association and other charities).

3. Within the UK the devolution process has led to calls for the Scottish Parliament to be given more responsibility over revenue raised and spent in Scotland. This was examined by the Calman Commission, which supported the principle and identified a number of taxes (Stamp Duty Land Tax, Landfill Tax, the Aggregates Levy and Air Passenger Duty, and proportion of Income Tax) where this could be applied. Under the Scotland Act 2012 the Scottish Parliament and the Scottish Government were given new tax and borrowing powers. The main changes introduced were:
   - the power to set a tax on land transactions and on landfill disposals (from April 2015);
   - the ability to borrow money for capital schemes (from April 2015); and
   - the right to set a Scottish rate of income tax for Scottish taxpayers across all tax bands (from April 2016).

4. The current UK Stamp Duty Land Tax and Landfill Tax will cease to apply in Scotland with effect from April 2015. UK Income Tax in Scotland will be reduced by 10p in the

pound with effect from April 2016. The previous UK Government had said in November 2009 that it would implement the Calman Commission recommendation that control of the Aggregates Levy should also be devolved to the Scottish Parliament. However this was not included in the Scotland Act 2012, although the Scottish Government has stated that it expects the Aggregates Levy to be devolved at some point in the near future.

Landfill Tax – The Current Position

5. The Landfill Tax has been in operation since 1 October 1996. It applies to all (non-exempt) material disposed of as waste, by way of landfill, at a landfill site which holds a Waste Management licence or a Pollution Prevention and Control (PPC) permit. Most sites are in fact covered by a PPC permit rather than a Waste Management licence. In 2010 (the most recent year for which there are published figures), there were 72 active landfill sites in Scotland, and 275 closed landfill sites.

6. Landfill Tax is paid by the landfill site operator. If the person responsible for the day to day operation of the site is a different person from the person named on the permit or licence as the controller of the site, then the actual controller of the site responsible for accepting or refusing material deposited in the site is jointly and severally liable for the tax. Tax is paid on any waste deposited in the site, including waste which the operator may have produced, unless it is exempt from tax.

7. Landfill material is brought onto the site and deposited in cells. The waste deposited in a cell each day is covered up with soil or other suitable material that day so as to prevent deposited waste being blown away, picked up and carried away by gulls or otherwise becoming a nuisance. The site is constructed so that gas and liquid from decaying material in the cells is taken away and treated for reuse or otherwise disposed of. When a cell approaches its capacity it is capped. Landfill Tax is chargeable by weight and is paid at two rates. There is a lower rate which applies to inert waste material [listed in the Landfill Tax (Qualifying Material) Order 2011, as amended]. This type of waste is considered have low risk of environmental harm. There is a higher rate, the standard rate, which applies to all other taxable waste. The standard rate for active waste is currently £64 per tonne, and the lower rate is £2.50 per tonne. The standard rate of landfill tax will increase by £8 per tonne in April 2013 and a further £8 per tonne in April 2014. There will be a floor under the standard rate at £80 per tonne, so that the rate will not fall below £80 per tonne from April 2014 until at least 2020. The lower rate will remain at £2.50 until at least April 2014, but there has been no announcement yet as to what level will apply to the lower rate from April 2014.

8. Landfill Tax becomes due either at the date the waste is disposed of to landfill (the disposal date), or alternatively at the date of invoicing if the invoice is issued within 14 days from the date of disposal (the invoice date).

9. Certain types of waste which are disposed of at landfill sites are exempt from being

charged in certain circumstances. The exemptions cover materials recovered from dredging inland waterways and harbours, waste arising from mining and quarrying activities, lower rated waste used to fill quarries, waste from visiting NATO forces in certain circumstances, and pet cemeteries. That last exception applies because dead domestic pets are treated as waste in the same way as any other dead animal under environmental law, and pet cemeteries themselves are treated as landfill sites. However, where a dead pet is buried at a pet cemetery it is exempt from tax. As long as the site is used only for the burial of dead pets the site operator is not required to register with HM Revenue & Customs for landfill tax. A former exemption for waste from the reclamation of contaminated land was withdrawn with effect from April 2012.

10. In *HMRC v Waste Recycling Group*, [2009] Env L R 5, [2009] STC 200 (the *WRG* case) the Court of Appeal held that otherwise discarded inert construction and demolition waste brought onto site by WRG and used for site engineering purposes, or in order to comply with site licensing conditions (such as daily landfill cover), was not liable for taxation as there had not been a 'disposal' for the purposes of Section 40 of the Finance Act 1996. Whilst there had been a disposal of the waste by the original producer, the Court said that there was no principle that material once labelled as waste was always waste just because the original producer of it threw it away. It considered that the relevant point in time to consider the matter was when the material arrived at the site. The Court found that by the time WRG's came to use this material at the site, the use was clear, and it was conclusive of its intention at the relevant time regardless of whatever means and on whatever terms they acquired it.

11. The reasoning of the Court of Appeal in the *WRG* case appears to contrast with that of Lord Menzies in *Landmore Limited v Shanks Dumfries and Galloway Limited*, 2012 SCLR 46. The *Landmore* case was about the construction of a lease entered into in 2004 of an area of ground used as a landfill site. The rent was to be calculated on the basis of an occupational rent and a royalty rent, *i.e.*, a payment in respect of the amount of waste entering the landfill site each day. The dispute between the parties was whether material sourced from construction sites operated by third parties, and which was brought onto the lease subject in order to create and cap the cells into which the waste was deposited, was itself 'waste' for the purposes of these royalty payments.

12. Lord Menzies emphasised that the exercise he was engaged in was the construction of a commercial document, and that this was not the same as construing an EU Directive or statutory regulations. Nonetheless Lord Menzies looked at a number of cases concerned with the definition of waste under European and domestic legislation (*Vissovo and Zanetti*, [1990] ECR 1-01461; *Scottish Power Generation Ltd v SEPA (No. 1)*, 2005 SLT 98; *H L Friel & Son Ltd v Inverclyde District Council*, 1995 SLT 1310; *Department of Environment and Heritage Service v Felix O'Hare & Co Ltd*, [2007] NICA 45) and he considered that the meaning of 'waste' as indicated by those cases was the meaning which the parties must have had in mind when negotiating and entering the contract. The ratio which Lord Menzies drew out from the cases that he was referred to was that

whether something could be defined as 'waste' was based on whether it was unwanted by the holder and therefore needed to be discarded or disposed of. The fact that there may be a commercial market for the material did not stop it being waste, and that until there was some physical process between the time of the material being discarded and the time that it entered the landfill site the material remained 'waste' for the purposes of the royalty payment clause in the lease.

13. In the *Landmore* case it can be seen that it was decided from the perspective of when the material was discarded. By contrast the Court of Appeal in *WRG* was looking at the issue from the point of view of why the material was being brought onto the site. Although the cases are about the definition of 'waste' on a landfill site within different contexts, it does seem to me that there is considerable sense in seeing these two contexts as overlapping. If the material is 'waste' for the purposes of a royalty payment in respect of what is being deposited at a landfill site, I would argue that it ought to be 'waste' for the purposes of paying Landfill Tax. Conversely, if the material is not taxable as waste, as was found to be the case in *WRG*, it seems odd that it should be subject to a royalty payment on the basis that it is waste..

14. In the *WRG* case HMRC was ordered to pay back the tax to WRG. It was suggested that this decision would result in approximately £300 million in Landfill Tax which had been wrongly paid by others having to be repaid. In practice it seems likely that the sums that will actually be repaid will be somewhat lower than this.

15. One reason why it seems likely that the amount of tax which will be repaid will be lower than the original headline figure can be illustrated by a tax tribunal ruling earlier this year which held that HMRC were not liable to repay landfill tax even though it was agreed that that the effect of the decision in the *WRG* case was that the appellant's activities were never taxable and that the sums paid to the Commissioners were not therefore due, *Harley v Revenue and Customs Commissioners*, [2012] UKFTT 66 (TC), (20 January 2012). The appellants sought to found on a letter dated 20 May 1998 as amounting to either a repayment claim (Finance Act 1996, Schedule 5, paragraph 14) or as a claim for credit in respect of tax that was due but where certain conditions applied which meant that a credit could be given for the activity carried out (Finance Act 1996, Section 51). In that letter the taxpayer asked that a proposed exemption to paying landfill tax should apply, and a promise to keep in touch with HMRC in view of the importance of the matter to him. The tribunal held that the claim for repayment was unsuccessful because the letter founded upon was not actually a claim for repayment, and by the time an express claim for repayment was made in 2009, a statutory three year time limit meant that such a claim was too late. The claim for credit was also unsuccessful because, although no time limit applied to such a claim and the demand for repayment in 2009 should be read as a claim for credit under Section 51, the wording of that section meant that it applied only to cases where tax was due (and contrasted with the wording of Schedule 5, paragraph 14). As the tax paid had in fact never been tax that was due, the Tribunal held that there was no entitlement to credit under Section 51. The effect of the decision seems ironic, because it

means that where tax is levied and paid but it is subsequently shown that the tax was not taken illegally the state is nonetheless entitled to hold on to the illegally taken tax unless a claim is made within three years of the unlawfully demanded payment. By contrast, there would be no time limit to a claim for payment of sums due by credit where the money was lawfully taken in the first place.

16. Indeed, instead of tax being repaid it now appears that landfill site operators will be paying more tax than they had anticipated. This follows from HMRC guidance issued in May, June and July 2012. The briefing issued in May (Brief 15/12) said that Landfill Tax should be paid on material known as 'fluff' (which is around a metre of material lying between the top of the normal landfill material and the final clay cap overlying each cell). This had formerly been treated as engineering material and not liable to Landfill Tax. The briefing also said that the 'trommel fines', grit and screening material from recycling processes would no longer be eligible for the lower £2.50 rate of landfill tax applied to inert material, and must be charged the standard rate of £64 a tonne. These changes were seen as something of a shock announcement when the briefing came out. HMRC's view is that the material forming the 'fluff' layer was always liable to Landfill Tax as it is waste material which is disposed of with the intention of discarding it, and the way it is used on the landfill site does not constitute a non taxable use of that material. HMRC have pointed to a change in the Landfill Tax (Prescribed Landfill Activities) Order 2009 which came into effect on 1 September 2009, which brought the fluff layer into the list of activities on the site liable to tax.

17. The other area where a change has been made is in relation to trommel fines, grits and screenings from waste transfer stations and recycling facilities. HMRC took the view that it was impossible to tell the source of these materials, and that they could be contaminated with asbestos, metal, wood, plastics or chemicals. As a result the Landfill Tax (Qualifying Material) Order 2011 made a change to the list of materials which attracted the lower rate of tax. The purpose of this was to remove materials which might be affected by contaminants from the lower rate of tax. The HMRC briefing 15/12 indicated that all such material would attract the standard rate of tax rather than the lower rate. This was later clarified by Brief 18/12 and a briefing document called *Interim Advice On Lower Rating*. The effect of these documents was to advise that so long as the material is one of the listed materials, and the conditions attached to the 2011 Order are met, the lower rate of tax will apply. The change means that qualifying materials which are contaminated by non-qualifying material will still attract the lower rate of tax, provided that there was only an incidental amount of non-qualifying material included. What this means in practice is unclear. Potentially it ought to mean that in order to attract the lower rate there will have to be an evidential record of what this material consists of in order to show that it does not contain any significant levels of contaminants. This should involve more work being done at recycling facilities to separate potentially contaminated material from uncontaminated material during the recycling process. The problem is that this does not really address the issue of unscrupulous operators who do not accurately measure the presence of contaminants and dump them in landfill. The changes made by the 2011

order were intended to clamp down on unscrupulous operators. The potential effect is that the burden has been increased on those who comply with the legislation whilst increasing the incentive for the unscrupulous to continue with their activities in the knowledge that it can be very hard to catch them once the material has been dumped and covered over.

The Consultation on replacing Landfill Tax in Scotland

18. The Scottish Government has had a long term strategy of developing Scotland as low carbon economy, reducing greenhouse gas emissions, and creating an economic development strategy based on sustainable economic growth. In the area of energy production these strategies have focussed on a well-publicised policy to produce 100% of Scotland's energy from renewable sources. The economic and emission reduction strategies are supported by the Zero Waste Plan.

19. Most recently the Waste (Scotland) Regulations 2012 gave effect to provisions in the European Waste Directive (2008/98/EC) which made changes as to how waste is collected and processed. The aim is to ensure so far as possible that any material that can be reused or recycled is reused or recycled. Where that cannot be done then the material should be used for energy production. Sending material to landfill ought to be a solution of last resort. The specific effect of these changes is that from 1 January 2014 there will be a duty on waste producers (except households) to collect dry recyclable waste separately, and a ban on such materials being sent to landfill or incineration. From 1 January 2016 food producers will have to separately collect food waste. From 1 January 2021 there will be a ban on biodegradable municipal waste going to landfill.

20. The Scottish Government is currently consulting on a Landfill Tax for Scotland. The Consultation Document is called *Protecting Our Resources*. In that document the Scottish Government has stated that it does not intend to make significant changes to the form or structure of Landfill Tax when introducing a replacement. It does set out what it sees as the core principles for guiding environmental tax policy in Scotland. These core principles are that:
    - environmental tax, or adjustment of existing taxes to promote sustainable use of resources, should only be considered where it can be demonstrated that it will help address or mitigate an environmental problem;
    - environmental tax should send a clear signal to both consumers and producers about outcomes sought; that signal is crucial for the long-term planning of companies and ensuring that environmental problems will be solved in the most economically efficient way;
    - environmental tax should not disadvantage Scottish companies, and lower income groups should not pay a greater share of the overall tax take.

21. At the moment the tax is collected by HMRC. In anticipation of acquiring a revenue

raising function, the Scottish Government announced the creation of a new agency called Revenue Scotland. A consultation on putting that new agency on a statutory basis was launched on 10 December 2012. The consultation can be found on the Scottish Government website at http://www.scotland.gov.uk/Publications/2012/12/5404 and will close on 12 April 2013

22. *Protecting Our Resources* proposes that the collection agent for a Scottish Landfill Tax should be the Scottish Environment Protection Agency (SEPA). The reason for this is that SEPA already has responsibility for permitting and regulating landfill sites, therefore it ought to be relatively simple to link the administration of Landfill Tax with the administration and enforcement of landfill permitting.

23. *Protecting Our Resources* raises a number of possibilities where Scotland might take a different approach to the taxation of landfill material. Questions included in the consultation document ask whether consideration should be given to the longer term introduction of new differential rates for stabilised materials or for combustion residues (bottom ash) from incineration, and whether tax which has been avoided by illegal dumping could be recovered from those responsible (in addition to environmental protection penalties)? In relation to this last question, it does appear that such power already exists under Part 3 of the Proceeds of Crime Act 2002. In *R v Allingham*, [2012] NICA 29 (29 June 2012) the Court of Appeal in Northern Ireland dismissed appeals against confiscation orders made under the Proceeds of Crime Act 2002 in respect of evasion of landfill tax and whether the appellants had obtained a pecuniary advantage were dismissed. The appellants were each the owners and operators of the sites where the waste was disposed of illegally. They were convicted of keeping controlled waste on land without a waste management licence. The confiscation orders included sums representing the amount received by way of payment charges from those who deposited the waste on the illegal landfill sites, the amount of Landfill Tax that would otherwise have been paid had the waste been disposed of at a lawful landfill site, and an amount to account for inflation between the date when the tax ought to have been paid and the date of the confiscation orders. The Court held that at the date the waste was discovered Landfill Tax was due on all the waste deposited there.

24. Other possible areas under consideration for change are a change in the tax point and possible changes to what is said to be taxable and what is not taxable. Although this latter point only talks about being clear, consistent and avoiding dispute, it does come across as an invitation to landfill operators to lobby the Scottish Government to undo some of the changes made in the 2009 and 2011 Orders that are referred to in paragraphs 16 and 17 above.

What Happens Next

25. The consultation on the Landfill Tax in Scotland closes on 15 January 2013. The consultation can be found at http://www.scotland.gov.uk/Publications/2012/10/3524.

After the consultation a Bill will be introduced in the Scottish Parliament in Spring 2013. There will be a separate Tax Management (Scotland) Bill to deal with procedural aspects of all aspects of the tax information gathering, penalties, rights of review and appeal process. The pre-Bill consultation for that will also start in the Spring with a Bill introduced in the Autumn of 2013 and expected to be passed by the Scottish Parliament by the Summer of 2014. The Land and Building Transaction Tax (Scotland) Bill should be enacted in the Summer of 2013, and the secondary regulations under that Act and the Landfill (Scotland) Tax would go through the Parliamentary process in the Summer of 2014.