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Advancing Pakistan's Climate Support Levy: Lessons from Global Carbon Pricing Models

Carbon Tax vs. Climate Support Levy

A **carbon tax** is a straightforward economic instrument that imposes a direct tax on carbon emissions, usually levied on fossil fuel producers or large-scale emitters. The tax is calculated based on the carbon content of fuels or the actual volume of greenhouse gas (GHG) emissions, thus creating a financial disincentive for pollution. Its core principle is "polluter pays," encouraging industries to shift toward cleaner technologies to avoid higher costs.

In contrast, a **Climate Support Levy**—sometimes referred to as a carbon levy in broader discussions—is not always linked directly to emission volumes. Instead, it is a broader fiscal mechanism imposed on carbon-intensive goods or services, often with the explicit goal of financing climate mitigation, adaptation, or energy transition programs. It may be collected at points of sale, import, or production and funneled into green infrastructure, renewable energy subsidies, climate resilience projects, or social safety nets for vulnerable populations affected by decarbonization.

Feature	Carbon Tax	Climate Support Levy
Basis	Volume of emissions or fuel carbon content	Price or type of carbon-intensive product/service
Purpose	Discourage emissions	Raise funds for climate-related initiatives
Direct Link to Emissions	Yes	Not necessarily
Use of Revenue	General revenue or earmarked	Typically earmarked for climate action

Climate Support Levy in Finance Act 2025

The Climate Support Levy, introduced in Pakistan's Finance Bill 2025–26 and effective from July 1, 2025, is a fiscal measure designed to address environmental and climate challenges through economic means. Initially labeled a carbon levy, the term was later changed to emphasize its broader developmental purpose. The levy imposes a charge of Rs. 2.50 per liter on petroleum products such as petrol, diesel, and furnace oil. It aims to discourage the excessive use of fossil fuels and simultaneously generate dedicated revenue for climate resilience projects, including green infrastructure, renewable energy initiatives, and environmental adaptation programs. By internalizing the environmental cost of carbon emissions, the Climate Support Levy marks a significant step toward integrating climate responsibility into the national fiscal policy.

New Energy Vehicles (NEV) Adoption Levy

The New Energy Vehicles Adoption Levy Act of 2025 is also part of the Finance Bill 2025–26—another forward-looking initiative aimed at transforming Pakistan's transportation sector. The Act imposes a 1% to 3% levy on all Internal Combustion Engine (ICE) vehicles, whether imported or locally assembled, while offering exemptions for electric vehicles (EVs), hybrids with at least 50 km electric range, and hydrogen fuel cell vehicles. The levy is collected at the import or manufacturing stage and is intended to fund the development of EV infrastructure, support the transition to clean transport, and reduce air pollution. By creating financial disincentives for traditional vehicles and channeling funds into sustainable alternatives, the NEV Adoption Levy supports Pakistan's broader climate commitments and green growth strategy.

Which Countries Have Implemented the Carbon Tax?

Singapore

Singapore's carbon tax offers a structured and phased model for implementing carbon pricing in an advanced, trade-exposed economy.

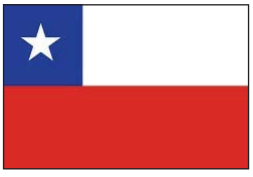
Key elements include:

- **Phased Tax Trajectory:** Introduced in 2019 at a carbon tax rate of five Singapore dollars per tonne of carbon dioxide equivalent (S$5/tCO$_2$e), Singapore's carbon tax is set to progressively increase to a range of 50 to 80 Singapore dollars per tonne of CO_2 equivalent (US$50–80/tCO$_2$e) by 2030. This gradual approach gives businesses time to adapt while strengthening the carbon price signal over time.
- **Broad Emissions Coverage:** The tax applies to facilities emitting over 25,000 tonnes of CO_2 annually, covering approximately 70% of the country's total emissions—one of the highest coverage levels globally.
- **Revenue Recycling for Green Transition:** Rather than generating net revenue, tax proceeds are reinvested in decarbonization initiatives and household support schemes, ensuring a just transition.
- **Support for Trade-Exposed Sectors:** A transition framework offers temporary allowances to emissions-intensive trade-exposed (EITE) industries to mitigate carbon leakage while incentivizing cleaner operations.
- **Carbon Credit Offsets:** From 2024, companies can offset up to 5% of emissions using high-quality international carbon credits aligned with Article 6 of the Paris Agreement.

Sweden

Sweden provides a strong example of the long-term benefits and practical outcomes of adopting carbon taxation policies. Key features include:

- **Significant Tax Levels:** Sweden implements one of the highest carbon tax rates globally—$127 per metric ton of CO_2—leading to substantial emissions reductions in regulated sectors.
- **Enduring Policy Approach:** Introduced in 1991, the longevity of Sweden's carbon tax has given businesses and citizens ample time to adjust and innovate.
- **Holistic Policy Mix:** The carbon tax is complemented by measures such as subsidies for renewable energy and strict energy efficiency standards, which collectively enhance its effectiveness.



Chile

Chile presents a developing country's approach to carbon taxation with expanding ambition. Key features include:

- **Initial Tax Coverage:** As of 2021, Chile's explicit carbon tax applied to 33.2% of national GHG emissions. A broader 55.8% of emissions were subject to a positive Net Effective Carbon Rate NER). Implicit pricing via fuel excise taxes covered an additional 5.9%, while fossil fuel subsidies remained at 1.6%.
- **Low Starting Rate:** Chile's carbon tax began at a modest rate of $5 per ton of CO_2, which limited its immediate environmental impact but created a foundational framework for future increases.
- **Future Scaling Scenarios:** In 2023, the IMF proposed four scaling options, ranging from a "moderate" path to US$15–50/tCO$_2$ (from 2025 to 2035) to a "social cost" approach of US$35–75/tCO$_2$ (US$35 in 2024 rising to US$75 in 2030). Other options included a hybrid model integrating an emissions trading system (ETS) and a base scenario excluding transport fuels but increasing fuel-specific levies over time.
- **Upward Pricing Strategy:** IMF encouraged Chile to maintain a steady, upward pricing trajectory and to ensure that revenues are reinvested to support communities and workers during the transition.

Malaysia

Malaysia is progressively advancing its climate strategy by integrating carbon taxation with voluntary carbon markets to meet both emissions and economic development goals. Key elements include:

- **Stepwise Carbon Pricing Evolution:** Malaysia launched its Voluntary Carbon Market (VCM) initiative in 2022, leading to the establishment of the Bursa Malaysia Carbon Exchange and its first carbon credit auction in March 2023. This market provides a transparent platform for pricing and trading carbon credits domestically.
- **Planned Carbon Tax Implementation:** As announced in Budget 2025, Malaysia plans to introduce a carbon tax by 2026, initially targeting the iron, steel, and energy industries. This tax aims to internalize carbon costs, stimulate cleaner industrial practices, and safeguard export competitiveness in response to the EU's Carbon Border Adjustment Mechanism (CBAM).

- **Nature-Based Solutions (NbS) Integration:** Malaysia's carbon credit market includes NbS, as seen in the Kuamut Rainforest Conservation Project, which generates high-integrity credits certified under the CCB Standards. These credits offer biodiversity and community co-benefits, demonstrating the potential for high-value, multi-benefit carbon assets from Malaysian forests.
- **Readiness for Broader Sectoral Expansion:** The carbon tax may be extended to other CBAM-affected sectors such as cement, aluminum, fertilizers, and hydrogen, aligning national policy with international trade and climate expectations.

How Pakistan Can Enhance Its Climate Support Levy

1) **Set a Clear Trajectory:** Adopt a multi-year roadmap to gradually increase the levy (e.g., from PKR 2.50/L to PKR 10 by 2030), sending a strong market signal like Singapore.
2) **Widen Sectoral Coverage:** Expand beyond fuel to include industrial and power sectors, similar to Malaysia and Chile—especially those exposed to CBAM.
3) **Enable Carbon Credit Offsets:** Allow partial offset of levy obligations through verified domestic carbon credits, encouraging investment in local mitigation projects.
4) **Link with a National Carbon Market:** Develop a Pakistan Carbon Exchange to trade credits transparently, supporting hybrid pricing models like Malaysia's VCM.
5) **Support Vulnerable Sectors:** Design transition frameworks to support energy-intensive exporters—a critical lesson from Singapore to avoid carbon leakage.
6) **Promote Nature-Based Solutions:** Incentivize reforestation, soil carbon, and wetland restoration with high-quality, co-benefit generating credits modeled on Malaysia's Kuamut Project.
7) **Revenue Recycling:** Earmark levy proceeds for clean energy transition, climate resilience projects, and social safety nets, reinforcing public trust.

Conclusion

Both carbon taxes and climate support levies play vital roles in steering economies toward lower-carbon pathways: the former directly prices emissions at their source, while the latter raises dedicated funds for resilience and clean-energy investments. Pakistan's new Climate Support Levy and NEV Adoption Levy demonstrate a pragmatic, phased approach mirroring global best practices to disincentivize fossil fuels, promote zero-emission transport, and mobilize revenue for green infrastructure. By setting clear price trajectories, widening sectoral coverage, enabling credible carbon-credit offsets, and reinvesting proceeds in a just transition, Pakistan can build on these foundations to achieve meaningful emissions cuts and sustainable growth. As other economies have shown, the effectiveness of these fiscal tools hinges on transparency, stable policy signals, and the integration of complementary measures that support industry adaptation and safeguard vulnerable communities.

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