



ENERGY TAX DIRECTIVE, PROMOTION OF RENEWABLE ENERGY AND STATE AID

Dr. D. Álvaro Antón Antón
ENDESA Chair of Taxation and Climate Change
Universidad CEU-Cardenal Herrera

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1. THE INHERENT LOGIC OF EU ETD

1. OCDE ENVIRONMENTAL TAXES DEFINITION =

- **A tax whose tax base is a physical unit (or a proxy of it) that has a proven specific negative impact on the environment. Four subsets of environmental taxes are distinguished: energy taxes, transport taxes, pollution taxes and resources taxes. Taxes should not be confounded neither with payments of rent nor with purchase of an environmental protection service.**

-In most instances the definition is derived from statistical standards developed by international organizations such as the IMF, OECD, Eurostat, ILO. Where possible, the definition has been quoted word for word from the source.

-Source Publication: United Nations, European Commission, International Monetary Fund, Organization for Economic Co-operation and Development, World Bank, 2005, Handbook of National Accounting: Integrated Environmental and Economic Accounting 2003, Studies in Methods, Series F, No.61, Rev.1, Glossary, United Nations, New York, paras. 2.102 & 6.26

2. ETD = ENVIRONMENTAL TAX?

INHERENT LOGIC OF ETD= LACK OF A TRUE ENVIRONMENTAL COMPONENT

Recital 22: “Energy products should essentially be subject to a Community framework when used as heating fuel or motor fuel. To that extent, it is in the nature and the logic of the tax system to exclude from the scope of the framework dual uses and non-fuel uses of energy products as well as mineralogical processes. Electricity used in similar ways should be treated on an equal footing”.

TRUE INHERENT LOGIC=

COLLECT REVENUES

PROTECT THE INTERNAL MARKET

THE ROLE OF EU MEMBER STATES ON “GREENING” ENERGY TAXES

- ❑ MITIGATE THE COST OF ENERGY INTENSIVE INDUSTRIES TO AVOID
 - Carbon Leakage
 - Coordinate ETS-ETD

= HIGHER ENERGY TAXES + CO2 TAXES

= *INDIRECT PROMOTION OF RENEWABLE ENERGIES*

- ❑ **DIRECT PROMOTION RENEWABLES ENERGIES**

EXCISE DUTIES TAX REDUCTION

ART. 15 ETD Electricity: solar, wind, wave, tidal
or geothermal origin;

ART. 16 ETD Transport Sector : BIOFUELS

Excise duty reductions

-Article 16(1) of the European Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity allows member States to apply an exemption or a reduced rate of taxation on biofuels.

-However, article 16(2) of the same Directive limits the exemption or reduction in taxation to the part of the product that actually derives from biomass. ***This means that for blended fuels the reduction may be applied to the biofuel component only.***

-Moreover, article 16(3) of the Energy Taxation Directive requires that the reduction in taxation shall be adjusted to take account of changes in raw material prices to avoid overcompensating for the extra costs involved in the production of biofuels.

The aim of this exception is reduce the final price of biofuels so they can compete with conventional petroleum-based fuels, making biofuel prices similar to the prices of the fossil fuels.

2. THE PROMOTION OF BIOFUELS IN THE EU CONTEXT

- *Directive 2009/28/EC, on the promotion of the use of energy from renewable sources and amending and subsequently repealing Directive 2003/30/EC.* =The Directive established a binding target for member States of 10% share of renewable energy in transport sector by 2020.
- That means that the Directive requires Member States to introduce legislation and take the necessary measures to ensure that, as from 2020, alternative fuels such as biofuels meet the target.
- However, as the production costs of biofuels are higher than the fossil fuels market prices, they cannot penetrate in the market by themselves. For this reason, the EU member States are supporting these products so they can compete with fossil fuels on the market.

MAIN SUPPORT SYSTEMS TO PROMOTE BIOFUEL IN THE EU

Member States main Support Systems to promote Biofuels in Transport Sector

		Austria	Belgium	Bulgaria	Cyprus	R. Czech	Germany	Denmark	Estonia	Spain	Finland	France	Greece	Hungary	Ireland	Italy	Lithuania	Luxembourg	Latvia	Malta	Netherlands	Poland	Portugal	Romania	Sweden	Slovenia	Slovakia	Utd .Kingdom
Transport	Quote Obligation	X		X	X	X	X	X		X	X	X			X		X	X	X		X	X	X	X		X	X	X
	Tax Exemptions	X	X		X	X	X	X	X			X	X	X	X	X	X	X	X	X		X	X	X	X	X	X	X

Source: EUROPEAN COMMISSION: *Renewable Energy: Progressing towards the 2020 target*, COM (2011) 31 final.

ADVANTAGES AND DISADVANTAGES OF EACH INSTRUMENT SEPARATELY :

<p>Tax exemptions</p> <p>(Production increases according to variations in relative prices)</p>	<p>Strengths</p>	<ul style="list-style-type: none"> -Easy to implement; -Few market risks; -Incentive for innovation; -Suitable for the early stages of development
	<p>Weaknesses</p>	<ul style="list-style-type: none"> -Loss of fiscal revenues; -Risks of overcompensation (if high tax reduction); -Strongly dependent on the initial levels of the excise tax: it is effective where these levels are high
<p>Quota obligations</p> <p>(The produce increases independently from variations in relative prices)</p>	<p>Strengths</p>	<ul style="list-style-type: none"> -It injects certainty into the agricultural sector; (unless the subsequent increase in prices significantly penalizes the agricultural supply) -It does not involve additional costs for public budget; -Suitable for the more advanced stages of development
	<p>Weaknesses</p>	<ul style="list-style-type: none"> -Higher prices for consumers; -<input type="checkbox"/> Less incentive to innovate; -Higher prices variability; -Difficult to implement and monitor
<p>Source: EUROPEAN COMMISSION: <i>The Renewable Energy Progress Report</i>, SEC (2009) 503 final</p>		

EU Commission studies the combination of tax exemption and "quota system" is the most successful option to achieve the EU biofuel target :

Shift in the measures used to support biofuels	Average annual growth rate of biofuels (%)
Replacing a tax relief system with an obligation to blend and a tax relief.	70%
Remaining with just a tax relief.	63%
Remaining with both measures (tax relief and obligation to blend).	49%
Replacing a tax relief system with just an obligation to blend.	36%
Source: EUREAN COMMISSION: <i>The Renewable Energy Progress Report</i> , SEC(2009) 503 final	

3. STATE AID ASPECTS

- Support schemes need to comply with rules on **State aid.**

Article 107.1 Treaty on the Functioning of the European Union

“Save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market”.

STATE AID PERSPECTIVE : divided between

Investment support (capital grants, tax exemptions or reductions on the purchase of goods)

Operating support (price subsidies, green certificates, tender schemes and tax exemptions or reductions on the production of electricity).

Article 107(1) of the Treaty on the Functioning of the European Union Lays down four conditions:

- It must confer an advantage on the recipient.
- It must be selective.
- The intervention must distort or threaten to distort competition.
- Transfer of State resources

3.1 STATE AID LAW AND THE EXCISE DUTY REDUCTION FOR BIOFUELS

- Exemption contained in the Energy Tax Directives (Directive 2003/96/EC) However, the Commission recalls that its competence on State aid issues originates directly from the TFEU. Therefore, any Community legislation cannot possibly impair the Commission's competence in this field.

❑ Existence of State aid

1 TRANSFER OF STATE RESOURCES

- ❑ measures are granted from State resources as they will directly reduce the tax resources otherwise paid to the State

2 ECONOMIC ADVANTAGE

- ❑ excise duty reduction is destined to alleviate costs incumbent on a specific sector, namely that of the production of certain biofuels.

3 SELECTIVITY

- ❑ by partly alleviating the tax debtors from the cost they normally would have to bear, the measure favours certain undertakings and the production of certain goods, namely biofuel producers.

4. EFFECT ON COMPETITION

- ❑ since biofuels serve as a substitute for fossil diesel and petrol, the advantage that biofuels producers receive with the tax reduction may distort competition in the internal EU market, and, because fuel and biofuel are widely traded between Member States, the measure is also likely to affect trade between Member States in this sector.

3.2 EU STATE AID LAW AND BIOFUEL SUPPLY OBLIGATION: Example of Spain

- In addition to the zero tax rate the Spanish government passed a new law in June 2007 (*Disposición Adicional Decimosexta de la Ley 34/1998 del Sector de Hidrocarburos*) to promote the use of biofuels in the transport sector. **According to this law fuel suppliers have to include a certain amount of biofuels in their overall sales.**

In order to reach the biofuel quota in a more efficient way Order ITC/2877/2008 was approved on the 9th October 2008: “which establishes regulations for the promotion of the use of biofuels and other renewable fuels in the transport sector”.

- + The Order sets an obligation on transport suppliers to supply a specified portion of their road fuel supplies to their customers in Spain from biofuels. (Specifically, the order set individual minimum targets per product, which are calculated as a percentage of their total road transport fuel sales).
- + Obligated parties are required to provide evidence of their compliance with the obligation to the Administrator appointed by the Order, which is the Spanish National Energy Commission (hereinafter NEC).
- + To provide some flexibility to suppliers the Order allows three options to comply with the supply obligation:
 - a) The first option is to comply with the obligation supplying eligible fuel from renewable sources (biofuels) to customers in Spain**
 - b) The second option is to comply with the supply obligation by buying Biofuels Certificates .**
 - c) The Order offers an alternative compliance mechanism based on a buy-out payment option rather than supply of biofuels.**

3.2 Existence of aid in the case of the supply obligation

Article 107(1) of the Treaty on the Functioning of the European Union Lays down four conditions:

- ✓ It must confer an advantage on the recipient.
- ✓ It must be selective.
- ✓ The intervention must distort or threaten to distort competition.
- **There must be an intervention by the State or through State resources?**

According to case-law, in order to be capable of being categorised as State aid a measure must:

First: be granted directly or indirectly through State resources

And

Second, be imputable to the State.

Judgment of the Court of Justice in Case C-482/99 *France /Commission* [2002] ECR I-4397, paragraph 24

State Resources NO INVOLVED

- Feed-in tariffs financed directly by private electricity suppliers who have to purchase electricity from green electricity producers at a price higher than the market price for electricity.
- The obligation to purchase a specific amount of green certificates seems comparable to the obligation to purchase electricity produced from renewable energy sources at fixed minimum prices, hence no State resources [State aid No N 362/2004 – United Kingdom Renewables Obligation Order 2005 (ROCs)]

- **Obligation to supply a share of biofuels. (State aid N 57/2008 Poland)**

The mere fact that supply obligation is imposed by statute and confers an undeniable advantage on certain undertakings (BIOFUEL PRODUCERS) is not capable to turn the private resources of the undertakings into State resources.

Public authorities at no stage enjoy or acquire control over the funds which finance the economic advantage in issue. (*Case C-379/98, PreussenElektra/Schleswig, judgement of 13.3.2001, [2001] ECR I-2099/ Conclusions of Advocate-General Jacobs in Case C-482/99 France v Commission [2002] ECR I-4397, paragraphs 38 to 42, and the judgment in Case C-379/98*)

- **Certificates = Not Aid**

- The State offers the obligated parties biofuel certificates for free.
- Hence the State offers them intangible assets.
- However, the State does not seem to foregone any revenues by offering the green certificates for free.

- **However**, In the Spanish system if obligated parties do not have a sufficient amount of biofuel certificates or are not able/willing to supply biofuels, they are obliged to pay the buy-out price to a fund.
- This fund will be redistributed in the end of the fixed period to obligated parties according to the number of biofuel certificates surrendered to the Administrators of the scheme.
- As a result, road fuel suppliers will receive an additional income through the redistribution of the fund. That means that the redistribution of the fund may favour some enterprises within the obliged group. Therefore, if the Commission ruled that State resources are involved, the redistribution of the fund might be considered State aid.
 - ❑ Must be determined whether the State exercised direct or indirect control over the resources in question, despite the fact that the funds did not come directly from the State budget.

The Court of Justice has held that :

- **The financial resources of a measure do not necessarily have to constitute permanent assets of the public sector in order for them to be categorised as State resources;**
- **Once resources came under State control, they remained State resources. The Commission considers, therefore, that the aid was granted directly or indirectly through State resources.**
- **It is sufficient that they constantly remain under public control and therefore available to the competent national authorities**

4. COMPATIBILITY OF THE AID WITH THE COMMON MARKET .

- The general principle of incompatibility is not absolute as articles 107 (2) and 107 (3) of the Treaty specify number of cases in which State aid could be considered acceptable.
- The Commission assessed the compliance of the support of renewable electricity with the Article 107(3)(c), particularly on the basis of the environmental aid guidelines.
- **New Community Guidelines on state aid for environmental protection**
- For national support measures which constitute State aid in the meaning of Article 107(1) of the EC Treaty, these rules establish the conditions under which Member States can grant financial support for the promotion of energy from renewable energy sources.

New Community Guidelines

No tax reductions for

- **Biofuels subject to a quota obligation**
- **Food-based biofuels**

Susanne Åkerfeldt

5. THE END OF TAX EXEMPTIONS FOR BIOFUELS : IS IT POSSIBLE TO EXTEND ITS APPLICATION?

- ✓ Tax reduction = temporary measure aimed to compensate the higher cost of biofuels production until they were competitive.
- Thus, before exemptions for biofuels are repealed it should be considered whether technological advances and changes in the price of raw materials allow them compete on equal footing with traditional fossil fuels without government intervention.
- In this respect, one could argue that, as a quota system is in force, the tax benefits are no longer required to facilitate the incorporation of these products to market.
 - ❖ From the point of view of the State aid prohibition established by art. 107 TFEU, this is one of the issues that create greater uncertainty when considering the possibility of extending the validity of these tax benefits.

- ✓ The extension of fiscal incentives is also conditioned by the decisions that may be taken by States for budgetary reasons.
- Under Directive 2009/28/EC each Member State must ensure compliance with the objective of 10%. = since the objectives of the Union in the field of biofuels are being reached and greater their role in the market, revenues from excise duties on energy would decrease.
- As the EU objective on biofuels can be achieved by other support systems that do not involve fiscal expenditure, i.e. “quota obligation”, it may be reasonable, from a tax collection standpoint, the replacement of such tax exemption with the “quota systems” rather than the joint application of both.
 - ❖ However, there are also reasons that justify further dispensing advantageous tax treatment to biofuels.

It should be understood that possibility opened by art. 16 of the ETD could act as a mitigation mechanism to the price increase experienced by fuels used in transportation, as a result of the obligation of blend these products with expensive ones such as biofuels.

6. CONCLUSIONS

- It would be appropriate to maintain some kind of tax reduction on energy taxation for biofuels, at least, until the ETD is revised by the Council in a way that takes into accounts the peculiarities of these products.
- Thus, the end of tax benefits for biofuels would have to be linked to the introduction of the necessary amendments in the ETD. This means that their end should be conditionally to the adaptation of energy taxes to the characteristics of these products in terms of their contribution to reducing CO₂ emissions and its lower energy content.