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COMMISSION STAFF WORKING DOCUMENT

Subsidiarity Grid

Accompanying the document

Proposal for a Council Directive

restructuring the Union framework for the taxation of energy products and electricity (recast)

{COM(2021) 563 final} - {SWD(2021) 641 final} - {SWD(2021) 642 final} -
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Subsidiarity Grid

1. Can the Union act? What is the legal basis and competence of the Unions' intended action?
1.1 Which article(s) of the Treaty are used to support the legislative proposal or policy initiative?
The proposal is based on Article 113 of the Treaty on the Functioning of the European Union (TFEU), which permits the EU to lay down harmonised rules in order to ensure the proper functioning of the internal market. This article provides for the Council, acting unanimously in accordance with a special legislative procedure and after consulting the European Parliament and the Economic and Social Committee, to adopt provisions for the harmonisation of Member States' rules in the area of indirect taxation. Additionally, appropriate provisions of fiscal nature intended, inter alia, to preserve and protect the environment can be adopted according to Article 192(2), first paragraph, of the TFEU.
1.2 Is the Union competence represented by this Treaty article exclusive, shared or supporting in nature?
In the case of taxation, the Union's competence is shared. Article 113 of the Treaty on the Functioning of the European Union provides that the Council shall adopt provisions for the harmonisation of legislation concerning excise duties to the extent that such harmonisation is necessary to ensure the establishment and the functioning of the internal market.
*Subsidiarity does not apply for policy areas where the Union has **exclusive** competence as defined in Article 3 TFEU[1]. It is the specific legal basis which determines whether the proposal falls under the subsidiarity control mechanism. Article 4 TFEU[2] sets out the areas where competence is shared between the Union and the Member States. Article 6 TFEU[3] sets out the areas for which the Unions has competence only to support the actions of the Member States.*
2. Subsidiarity Principle: Why should the EU act?
2.1 Does the proposal fulfil the procedural requirements of Protocol No. 2[4]: - Has there been a wide consultation before proposing the act? - Is there a detailed statement with qualitative and, where possible, quantitative indicators allowing an appraisal of whether the action can best be achieved at Union level?
The present proposal has been formulated taking into account a wide range of external contributions. Stakeholders were consulted first via the Inception Impact Assessment feedback mechanism and then via a dedicated Public Consultation. The public consultation was open from 22 July 2020 to 14 October 2020. In total, 563 responses from 25 Member States and from 5 third countries were received, together with 129 position papers. Besides the public consultation, direct consultations with Member States, including requests for input in view of the computation of effective tax rates, as well as with other stakeholders were also undertaken. An external study on the taxation of the aviation has also been commissioned by DG TAXUD for the purpose of the impact assessment.
2.2 Does the explanatory memorandum (and any impact assessment) accompanying the Commission's proposal contain an adequate justification regarding the conformity with the principle of subsidiarity?

[1] https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12008E003&from=EN
[2] https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12008E004&from=EN
[3] https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:12008E006:EN:HTML
[4] https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12016E/PRO/02&from=EN

The proposal falls under shared Union and Member State competence. Therefore, the subsidiarity principle applies. Article 113 of the Treaty on the Functioning of the European Union provides that the Council shall adopt provisions for the harmonisation of legislation concerning excise duties to the extent that such harmonisation is necessary to ensure the establishment and the functioning of the internal market. Additionally, appropriate provisions of fiscal nature intended, inter alia, to preserve and protect the environment can be adopted according to Article 192(2), first paragraph, of the TFEU
The proposal for the revision of the ETD and its timing need to be seen in the broader context of the EU energy and climate change agenda. The objective to bring the ETD more closely in line with the EU objectives and goals in this field can only be implemented by means of an act adopted by the Union, recasting the ETD.

2.3 Based on the answers to the questions below, can the objectives of the proposed action be achieved sufficiently by the Member States acting alone (necessity for EU action)?

The contribution of taxation to the European Green Deal climate and environmentally-related objectives can be ensured most adequately at the EU level. In fact, only a harmonised framework can help to attain the EU levels of ambition in these areas while seeking to preserve both the competitiveness of the productive sectors and the adequate level playing field among sectors and energy uses. Similarly, the EU's contribution to achieve higher climate ambitions globally will be most effective if the EU coordinates all the possible policy instruments, including taxation, in the context of an ambition plan, which encompasses also the extension of the ETS and other relevant policy actions. Member States acting alone cannot achieve the objectives of the proposed action.

(a) Are there significant/appreciable transnational/cross-border aspects to the problems being tackled? Have these been quantified?

The Energy Taxation Directive (ETD) is predominantly a single market directive so the great majority of the issues at stake are of a cross-border nature. There are no global quantified cross-border impacts of the inharmonious application of the ETD due to the complexity of framework and the flexible application throughout the EU. However, it is recognised that motor fuels that can be easily and legally transported across borders. If the final prices in the neighbouring states vary significantly, it creates an incentive to consumers crossing borders in order to refuel their vehicles at lower prices (tank tourism) in bordering regions thus depleting revenues in one Member States while inflating in another. The extent of this phenomenon, while observable, is nevertheless of a local nature.

(b) Would national action or the absence of the EU level action conflict with core objectives of the Treaty[5] or significantly damage the interests of other Member States?

It could happen, particularly in the frontier regions of countries with significantly diverging frameworks, including effective tax rates. If the Member States apply highly divergent national rates, in particular in combination with a wide range of tax exemptions and reductions, they create a risk of distortion of the level playing field across the involved sectors of the economy and an erosion of the tax base in high-taxing countries, notably for motor fuels that can be easily and legally transported across borders as explained above. The harmonisation of energy taxation through the Energy Tax Directive should contribute to avoid the harmful effects of energy tax competition between the Member States, stemming for example from the relocation of consumers of energy (in particular businesses) to Member States with more beneficial tax regimes.
Besides, without coordinated effort and same goals in perspective, the actions of one Member State could be threatened, or neutralised, by the lack of similar action – or, in worst case scenario, a contrary action – by another Member State.

[5] https://europa.eu/european-union/about-eu/eu-in-brief_en

(c) To what extent do Member States have the ability or possibility to enact appropriate measures?

Under the existing provisions, Member States can increase the rates of their energy taxes, decide not to make use of possible exemptions and reductions or introduce climate related objectives. They are in principle free to set the levels of taxation as they please as long as the minimum levels specified in the Directive are respected. However, such national approaches risk distorting the internal market and undermining the Green Deal objectives due to the non-harmonised structure and level of the national taxes. The Member States would need to multilaterally approximate their rates to create a more even level playing field but that is unlikely to happen as the directive leave a great room for manoeuvre and the Member States fix their rates in the context of their national energy, climate, fiscal and social policies. Since the actions of any given economic agent, including a state, are driven by own interest, in order to preserve the internal market, a framework of common acceptable rules with common acceptable minimum rates would preserve the interest of the EU as a whole.

(d) How does the problem and its causes (e.g. negative externalities, spill-over effects) vary across the national, regional and local levels of the EU?

Some problems are indeed accentuated in frontier areas between neighbouring Member States, where there was evidence of relocation of the consumption of motor fuels and heating fuels. For example, Member States have the possibility of setting national rates above the minimum levels defined in the ETD, resulting in highly divergent national rates for transport fuels. These differences induced a phenomenon of consumers crossing borders in order to refuel their vehicles at lower prices (tank tourism) in bordering regions. This indicates local distortion of competition while in all conformity with the current framework.

(e) Is the problem widespread across the EU or limited to a few Member States?

The Energy Tax Directive is predominantly a single market directive and most of its shortcomings relate to the functioning of the internal market as a whole. The directive does not affect all the Member States in the same way given its ample scope for flexibility of its application, depending on national prerogatives. In general, two groups of Member States can be distinguished:

- a group of "low-taxing Member States", typically taxing at rates close to the minima and having had often, although not in all cases, introduced taxation only as a consequence of the existence of common minimum rates;
- a group of "high-taxing Member States" with tax levels more or less clearly above the minima. For these countries the existence of common minima is particularly important to reduce competitive disadvantages for their industry. These countries also often make use of the possibility to apply reduced rates for energy-intensive businesses.

(f) Are Member States overstretched in achieving the objectives of the planned measure?

Measures at Member State level alone would not be able to achieve the objectives of the proposed initiative or the objectives of broader EU policies. Any future natural alignment across the EU Member States would likely be a lengthy and inefficient process.

(g) How do the views/preferred courses of action of national, regional and local authorities differ across the EU?

One of the main concerns raised by the stakeholders relates to the relevance of the current ETD in terms of its static definition of energy products and electricity. The consultation conducted in the course of evaluation of the ETD also revealed that national authorities and economic operators are generally in favour of bringing new products under the coverage of the ETD, mostly to ensure equal

tax treatment of different products for the same use. At the same time, no Member State or economic operator was in favour of excluding any further energy products or uses, which are currently covered by the ETD.
In some cases economic operators were motivated to include new products and uses into the scope of the ETD in order for those to be covered by exemptions and reductions. Although the ETD qualifies many of those products as taxable if used as motor fuel or for heating purposes, it does not provide any clear legal framework for the exemption of these alternative products used for similar purposes, as its provisions on exemptions and reductions mostly contain explicit references to energy products and electricity.

2.4 Based on the answer to the questions below, can the objectives of the proposed action be better achieved at Union level by reason of scale or effects of that action (EU added value)?

(a) Are there clear benefits from EU level action?

Yes. The absence of an increase in minimum rates for more than a decade at EU level has eroded the tax-induced price signal that was supposed to encourage investment in energy-efficient technology and behaviour. Moreover, as some Member States have increased their national level of taxation since then while others have not, there is risk of growing distortion of competition in the single market and an erosion of the tax base in high-taxing countries, notably for motor fuels that can be easily and legally transported across borders. In spite of repeated Commission calls for a shift in the taxation from labour to environmental taxes, the overall percentage of tax revenues from environmental taxes in the EU has remained relatively unchanged over the last decade.
Another consideration concerns the current' directive's scope, the static definition of energy products and the evolving energy mix. The ETD was adopted long before the emergence of new technologies and uses that are predicted to become important building blocks on the path to the EU's decarbonised future. As a result, the current ETD regime is not properly devised to ensure the preferential treatment of these new energy products and applications. In the worst cases, uncertainties resulting from the ETD hinder investment in low-carbon technologies. By default, the ETD applies standard tax treatment to electricity and biofuels, without differentiating between renewable and fossil fuel based electricity or the environmental performance of biofuels. In the absence of differentiation of biofuels in the ETD, Member States would continue applying their own, often diverging classifications, which on top of it often cannot be applied to the characteristics of biofuels produced in other Member States. Clearly, a common agreed framework for definition and treatment of energy and energy products would be by far more predictable, stable and less distortion-prone than individual actions by even group of Member States.

(b) Are there economies of scale? Can the objectives be met more efficiently at EU level (larger benefits per unit cost)? Will the functioning of the internal market be improved?

It is not about the economies of scale but about a coordinated approach and harmonised rules. The rules set out currently are no longer adapted to the new climate change and energy policy framework and contain several shortcomings from the perspective of the proper functioning of the internal market and in relation to the needs of the other EU policies. In particular energy and climate policies and initiatives have substantially developed since the ETD's adoption. The EU and its Member States have committed to swiftly and fully implement the Paris Agreement, to contribute to the fulfilment of sustainable finance goals, and to continue to lead in the fight against climate change. Taxation is set to play an important role in the achievement of these objectives but without a well designed EU framework, it will not happen.
For example, the share of the ETD minimum in industrial prices has become insignificant and thus not

allowing for a positive contribution to the functioning of the EU internal market. Thus, the potential of the ETD to reinforce core EU policies aimed at driving progress towards the completion of the internal market remains untapped unless this is uniformly corrected throughout the entire EU.
As put forward by the Commission in its 2018 Communication on a "Clean Planet for all - A European long-term strategic vision for a prosperous, modern, competitive and climate neutral economy", taxation and climate action and energy policies should be aligned. This was reiterated in the 2019 Commission Communication, where it was stressed that a future energy taxation framework should: (i) support the clean energy transition; (ii) contribute to sustainable and fair growth; and (iii) reflect social equity considerations.

(c) What are the benefits in replacing different national policies and rules with a more homogenous policy approach?

The proposal does not intend to replace national policies and rules but to approximate approach, coverage and tax treatment of energy and energy products across the EU to preserve the internal market. The ETD sets (only) the minimum levels of taxation. Member States are free to set their respective rates above these minima and introduce additional taxes, without an upper limit. These minimum rates have not been updated since the ETD was adopted, nor are they indexed to external developments such as inflation or a CO2 benchmark. As a result, they have remained unchanged since the adoption of the current Directive, which has led to an erosion of the impact of minimum rates as well as to the increasingly diverging national implementation of nominal tax rates. Bringing the minima to the levels corresponding to the contemporary conditions and broader policy objectives would provide the safety net for the internal market and prevent race-to-the-bottom and unfair competition between Member States (and sectors). The current directive is no longer fit to achieve this purpose.
The ETD also lists possible reductions and exemptions. The conditions under which these can be granted are defined very broadly, resulting in highly divergent national implementation of exemptions and reductions. Beyond the discretionary application of exemptions and reductions, the discretionary implementation of other provisions also undermine the objective of harmonisation. Such include: uncertainty in the application of the control and movement provisions and the definition of the conditions establishing the chargeable event. A divergent interpretation and implementation of these provisions may be an obstacle to the free movement of goods and investment capital.
For example, in some Member States, exemptions and reductions granted to large industrial users, result in an effective rate 90% lower than the nominal rate. In other Member States, the impact of reductions for the same type of consumer is limited to below 5%.
Moreover, as highlighted in the Communication, the presence of sector-specific energy tax exemptions or reductions, notably in the aviation, maritime and road haulage sectors and for energy-intensive industries, in general substantially weakens the incentives for investing in more energy-efficient capital stock and production processes in these sectors. These tax exemptions or reductions also constitute a burden for other sectors and/or private households that have to make up the revenue shortfalls triggered by them. Furthermore, they may distort competition between industrial sectors and may promote inefficient and polluting modes of transport.

(d) Do the benefits of EU-level action outweigh the loss of competence of the Member States and the local and regional authorities (beyond the costs and benefits of acting at national, regional and local levels)?

The flexibility principle would remain for member States as they would still be allowed to apply some exemptions and set rates freely as long as they stay above the minima. The competence transfer would be limited to agreeing on a common set of definitions and coordinated treatment of energy and energy products for tax purposes, including agreed minimum rates. Revision of the energy

taxation rules would help to address global challenges, expressed also in the EU strategic policies, starting with the European Green Deal's climate neutrality objectives as well as energy market integration, bringing ultimate benefits to all EU citizens. Therefore, acting at the EU level will enable to support and reinforce the cooperation of all the Member States in contributing to the achievement of key energy and climate policy objectives.

(e) Will there be improved legal clarity for those having to implement the legislation?

Yes. The high divergence of national frameworks for taxation of energy and energy products adds to the complexity of the system and increases uncertainty for the businesses. Such issues are nevertheless case specific and depend on the nature and geographical scope of activities of any given business. The main shortcomings with regard to clarity and completeness of provisions as well as structure of the ETD include: eleven cases of late transposition, outdated classification under the Combined Nomenclature (CN), and lack of clarity of several provisions of the ETD.

Albeit the ETD allows for the update of CN codes, such updates cannot result in the addition or removal of products from the scope of the ETD. Since the technology advanced and the energy market exhibits an array of new products not included in the current directive, a section of the energy and energy products market is unregulated. Bringing the new products into the scope of the directive would provide common definitions, approach and this increase the certainty for businesses, amongst other improvements.

In relation to the clarity of the ETD, different national interpretations emerged for specific provisions. These include: definition of taxable products; tradable permit schemes; definitions of the uses which are out of the scope – mineralogical and metallurgical processes; or interpretation of the exemption related to motor fuels used in air and water navigation, etc. There is also the need to align the terminology of the ETD with case-law by the CJEU. Following the adoption of the Directive the CJEU has clarified the interpretation of certain provisions. As a result, the text of the Directive and the Court's interpretation could lead to diverging application of the ETD by the Member States and to different understanding by the economic operators.

For example, in the absence of differentiation of biofuels in the ETD, Member States apply their own classifications. These are often diverging or cannot be applied to the characteristics of biofuels produced in other Member States. As a result, economic operators have no certainty whether preferential tax treatment applies to their products in other Member States. This might create an insecure business environment for biofuel producers operating across borders.

In addition, removing provisions that are no longer applicable, would improve the clarity of the legislation.

Finally, provisions governing exemptions and reductions are not presented in the ETD in a structured way. Instead, such provisions are spread across the Directive, with some sectors, such as energy intensive industries, being subject to multiple provisions contained in various sections of the legislation.

3. Proportionality: How the EU should act

3.1 Does the explanatory memorandum (and any impact assessment) accompanying the Commission's proposal contain an adequate justification regarding the proportionality of the proposal and a statement allowing appraisal of the compliance of the proposal with the principle of proportionality?

The proposal complies with the proportionality principle for the following reasons.

The objectives of the current proposal are best achieved by recasting the current Directive to the effect explained above. The proposal is mainly concerned with some essential components of the Directive: the structure of taxation and the relationship between the respective tax treatment of the various energy sources.

The proposal is in all respects limited to what is necessary in order to achieve the objectives pursued.
3.2 Based on the answers to the questions below and information available from any impact assessment, the explanatory memorandum or other sources, is the proposed action an appropriate way to achieve the intended objectives?
(a) Is the initiative limited to those aspects that Member States cannot achieve satisfactorily on their own, and where the Union can do better?
Yes. In the absence of EU level action, Member States would find it very difficult to coordinate enough and quickly enough respond to the global needs and challenges. It should be presumed that national interest would prevail over the ones of the EU as a community of states. In the worst case scenario, the diverging directions of Member States actions could lead to compromising other Member States efforts or to deepen the fragmentation of the internal market. The revised EU framework for taxation of energy and energy products would not deprive the Member States of their competence to design and run their energy and fiscal policies as long as they respect the minimum rates and common basic definitions and treatment of energy and energy products.
(b) Is the form of Union action (choice of instrument) justified, as simple as possible, and coherent with the satisfactory achievement of, and ensuring compliance with the objectives pursued (e.g. choice between regulation, (framework) directive, recommendation, or alternative regulatory methods such as co-legislation, etc.)?
Proposed instrument: Directive. In this area already covered by an existing Directive, Member States should continue to retain an important margin of flexibility. Other means than a Directive amending Directive 2003/96/CE would thus be inadequate.
(c) Does the Union action leave as much scope for national decision as possible while achieving satisfactorily the objectives set? (e.g. is it possible to limit the European action to minimum standards or use a less stringent policy instrument og approach?)
Yes. Member States will still be given the flexibility necessary to define and implement policies appropriate to their national circumstances. Within the new framework, they can still design fiscal arrangements made in connection with the implementation of the directive. In this regard, Member States might decide not to increase the overall tax burden if they consider that the implementation of such a principle of tax neutrality could contribute to the restructuring and the modernisation of their tax systems. For example, it is left entire up to the Member States to decide if and how the additional revenue from energy taxation could be used to reduce labour costs (e.g. by lowering social contributions). The instrument proposed – a Directive – as already described above, provides the best trade-off between non-interventionist EU policy, providing framework for approximation and coordination rather than full harmonisation, thus being the right vehicle to achieving the Union objectives recapitulated under the Green Deal. A more stringent instrument would unnecessarily restrict the Member States room for manoeuvre when it comes to implementation of national interest-driven policies. A weaker one, would risk not improving the status quo.
(d) Does the initiative create financial or administrative cost for the Union, national governments, regional or local authorities, economic operators or citizens? Are these costs commensurate with the objective to be achieved?
Some regulatory costs (mostly managing authorisations, declarations and IT systems update) will

arise for the traders in energy products newly introduced in the ETD's scope and for administrations as these products will be subject to some provisions of the excise general arrangements. However, these costs should be limited for hydrogen and solid biomass traders as these products will be allowed the same movement control simplifications as natural gas and coal respectively. The termination of excise duty exemptions for some fuels or sectors of activity (e.g. aviation and maritime) does not change the regulatory costs related to general arrangements as exempted fuels were anyway subject to holding and movement controls.
(e) While respecting the Union law, have special circumstances applying in individual Member States been taken into account?
Yes as part of the impact assessment the Commission analysis reflected, to the extent possible, the economic and industrial structures of individual Member States