Ref. Ares(2020)1350088 - 04/03/2020

European Commission

INCEPTION IMPACT ASSESSMENT

Inception Impact Assessments aim to inform citizens and stakeholders about the Commission's plans in order to allow them to provide feedback on the intended initiative and to participate effectively in future consultation activities. Citizens and stakeholders are in particular invited to provide views on the Commission's understanding of the problem and possible solutions and to make available any relevant information that they may have, including on possible impacts of the different options.

TITLE OF THE INITIATIVE	Revision of Directive 2003/96/EC restructuring the Community framework for the taxation of energy products and electricity (Energy Taxation Directive or 'ETD' or 'Directive')
LEAD DG (RESPONSIBLE UNIT)	DG TAXUD (C2)
LIKELY TYPE OF INITIATIVE	Legislative initiative
INDICATIVE PLANNING	*June 2021*
ADDITIONAL INFORMATION	*in the field*

The Inception Impact Assessment is provided for information purposes only. It does not prejudge the final decision of the Commission on whether this initiative will be pursued or on its final content. All elements of the initiative described by the Inception impact assessment, including its timing, are subject to change.

A. Context, Problem definition and Subsidiarity Check

Context

The **Energy Taxation Directive 2003/96** lays down the EU rules for the taxation of energy products used as motor fuel or heating fuel and of electricity. However, since its adoption in 2003, energy markets and technologies in the EU have experienced significant developments, and the EU's international commitments, including the Paris Agreement, as well as the EU's regulatory framework in the area of energy and climate change, have evolved considerably since then. This is confirmed in the evaluation that the Commission services published in September 2019[1] and recognised by the Council Conclusions adopted by the EU Finance Ministers at the ECOFIN meeting of 5 December 2019[2].

In 2011, the Commission already presented a revision of the present Directive with a view, among others, to better align the Directive to the energy market and climate challenges. After inconclusive discussions, the Commission withdrew its proposal in 2015.

The **European Green deal** adopted by the Commission on 11 December 2019 aims to transform the EU into a modern, resource-efficient and competitive economy where there are no net emissions of greenhouse gases in 2050 and where economic growth is decoupled from resource use. It includes increasing the EU climate ambition towards 50-55% GHG emission reductions for 2030. This requires effective carbon pricing and the removal of fossil fuel subsidies. Well-designed taxes play a direct role by sending the right price signals and providing the right incentives for sustainable practices of producers, users and consumers. The revision of Energy Taxation Directive forms part of a group of policy reforms to deliver on the increased ambition for 2030. The revision is an integral part of the European Green Deal and should therefore focus on environmental issues.

Problem the initiative aims to tackle

1. Persistence of fossil fuel subsidies: Highly divergent national rates are applied in combination with a wide range of tax exemptions and reductions in order to safeguard the competitiveness of EU industries and

[1] Commission report: evaluation of the Energy Taxation Directive, SWD(2019) 329 of 11 September 2019
[2] https://data.consilium.europa.eu/doc/document/ST-14861-2019-INIT/en/pdf

economies as well as to pursue other national policies. The wide range of exemptions and reductions are de facto, forms of fossil fuel subsidies, which are not in line with the objectives of the European Green Deal. These concern important sectors, such as aviation and maritime transport that are currently fully exempt from energy taxation, while land transport bears an important burden of energy taxation. All this increases the fragmentation of the internal market and in particular distorts the level playing field across the involved sectors of the economy. In addition, there are some aspects of the ETD that lack clarity, relevance and coherence.

2. The ETD is not in line with EU policy objectives: There is a lack of alignment between the ETD and, among others, the EU Emission Trading System, the Renewables Directive and the Energy Efficiency Directive. The Directive does not adequately promote greenhouse gas emission reductions, energy efficiency, or alternative fuels (hydrogen, synthetic fuels, e-fuels, advanced biofuels, electricity, etc.). The ETD does not provide sufficient incentives for investments in clean technologies. The treatment of the business sector, in particular energy intensive business and manufacturing sectors, under the ETD varies considerably. For the same reasons, the ETD is not in line with the objectives of the European Green Deal.

3. Lack of relevance for the internal market: The ETD does not achieve anymore its primary objective in relation to the proper functioning of the internal market, as the minimum tax rates have lost their effect. In the absence of an indexation mechanism, their real value has eroded over time and they no longer have a converging effect on national rates as the vast majority of Member States tax most energy products and, in some cases electricity, considerably above the ETD minima.

Basis for EU intervention (legal basis and subsidiarity check) [max 10 lines]

The legal basis of the present Directive is Article 113 of the Treaty of the Functioning of the EU that provides for a special legislative procedure whereby the Council acts unanimously. In line with the European Green Deal communication, the review of the directive should focus on environmental issues. Therefore, it is possible to use Article 192 of the Treaty (environmental measures including measures of fiscal nature) that allows European Parliament and the Council to adopt proposals in this area through the ordinary legislative procedure by Qualified Majority Voting rather than by unanimity in the Council.

Considering that existing harmonised EU rules are covered in an EU Directive, EU action is needed to tackle the shortcomings identified in the evaluation of the ETD. A number of Member States and the Council conclusions on the ETD evaluation adopted on 5 December 2019 have also requested the Commission to act. Member States alone will not be able to deliver the expected benefits of co-ordinated EU action.

B. Objectives and Policy options [max 20 lines]

The main objectives of the review of the ETD are:

i) Aligning taxation of energy products and electricity with EU energy and climate policies with a view to contributing to the EU 2030 targets and climate neutrality by 2050 in the context of the European Green Deal.

ii) Preserving the EU internal market by updating the scope and the structure of rates as well as by rationalising the use of optional tax exemptions and reductions by Member States.

The policy options outlined below do not preclude the possibility that alternative approaches may emerge through further stakeholder consultations – including public consultation - and studies.

The starting point for the exercise will be continuation of the current Directive in the context of the new baseline scenario of the European Green Deal and its higher ambition for 2030.

The Commission will develop a number of policy options based on the following building blocks. Dedicated options might be proposed for the aviation and maritime sectors:

1. The minimum excise rates – the review will take into account various aspects impacting excise rates, such as inflation, energy content (to make energy taxation least distortive possible), link to greenhouse gas emissions (to complement the price signal outside the EU Emission Trading System) in order to better align the minimum tax rates to the EU's climate and energy policies.

2. Sectoral tax differentiation - the review will consider motor fuel vs. heating fuel differentiation, revising and streamlining the current possibilities to apply differentiated rates, exemptions and reductions, e.g. for the maritime and aviation sectors which currently exempt aviation kerosene and fuel used by ships from taxation. The focus will be on tackling fossil fuel subsidies and avoiding inconsistencies between taxation and, among others, the Emission Trading System as well as the Renewables Directive and the Energy Efficiency Directive.
3. Product coverage. The use of a number of new energy products is currently discouraged since they can be taxed in the same way as the traditional ones (e.g. advanced alternative fuels in transport, which can include electricity). In this context, the Commission will also analyse how best to reconcile the energy and climate objectives with the objective of generating tax revenue.

Moreover, clarifying, updating and possibly revising definitions, also in relation to the applicability of control and movement provisions as well as on chargeable event and payment in certain cases (e.g. for batteries), and reconsidering the scope of the ETD, also as regards the uses out of scope, will also be addressed.

The review of the ETD is part of a series of measures announced in the European Green Deal, which also includes, among others, the review of the Emissions Trading System Directive; Effort Sharing Regulation; Land use, land use change and forestry Regulation; Energy Efficiency Directive; Renewable Energy Directive; CO2 emissions performance standards for cars and vans; Alternative Fuels Infrastructure Directive.

C. Preliminary Assessment of Expected Impacts [max 20 lines]

Likely economic impacts

The measures proposed would strengthen the level playing field across the EU internal market while contributing to the climate and energy policy goals of the EU. The measures proposed should not create any considerable regulatory burden or cost for the Member States, nor for economic operators.

The impact assessment accompanying the Commission proposal of 2011 withdrawn in 2015, showed that the macroeconomic impacts of reforms aimed at aligning the taxation of energy products and electricity with EU energy and climate policies are essentially driven by how Member States use existing and possible additional revenue. If the revenue is recycled through reductions in labour costs, effects on GDP and employment are always positive, although limited in size.

The measures could incentivise the investments in new technologies and the use of alternative, more sustainable energy products and electricity.

In line with the Council conclusions of December 2019, the economic impact as well as the social and environmental cost and benefits will be carefully assessed for competitiveness, connectivity, employment and sustainable growth, particularly for sectors most exposed to international competitiveness.

Likely social impacts

The measures could have possible direct impact because of possible revision of rates and of the exemptions and reductions for households and industry. While tax increases for fossil fuels in the transport or heating sector are powerful incentives towards behavioural change, in the short term, consumers may not be easily able to change their consumption patterns when an important share of their income is involved. This will be carefully assessed.

The final impact depends on the way in which the redistributive effect is compensated via accompanying measures through social policy and welfare systems. The reduction of other taxes (e.g. taxes on labour) or direct compensation to the lower income could compensate for the possible undesirable distributional effect of potential energy tax increases. Moreover, the Green Deal Investment Plan and the Just Transition Mechanism will contribute to address the transition needs for investment, including in the most affected areas. The European Green Deal also foresees measures to address energy poverty.

The Commission 2011 proposal for an ETD revision was not found to produce negative income effects, but the distributional impact would vary according to the method of revenue recycling chosen. Although labour-tax recycling produces the best overall results for household income, it tends to favour higher income over low-income households. Lump-sum recycling avoids regressive distributional effects though at the cost of producing a slight overall income decrease. A parallel increase in transport costs mitigates regressive distributional impacts of heating cost increases.

Likely environmental impacts

The environmental impact is expected to be positive both directly (immediate reduction in GHG and other pollutant emissions) and indirectly through stimulating investments into clean energy as well as energy saving and sustainable transport technologies.

Likely impacts on fundamental rights

No impact on fundamental rights is expected.

Likely impacts on simplification and/or administrative burden

The evaluation of the Energy Tax Directive concludes that the existence of fuel taxation did not lead to any considerable regulatory burden or costs for the Member States or the economic operators.

The clarifications and simplifications proposed for the definition of the scope of the Directive would further reduce the regulatory burden.

D. Evidence Base, Data collection and Better Regulation Instruments

Impact assessment

An impact assessment is being prepared to support the preparation of this initiative and to inform the Commission's decision. The impact assessment will be based on existing and "ad hoc" planned studies concerning, for instance, the internalisation of external costs in the transport sector, the comparisons of effective tax rates both for Member States and economic sectors, new technologies and alternative fuels, the impact of the application of the Directive on energy intensive sectors. It will also rely on the findings of the parallel impact assessments on the revision of the ETS and on the review of the Directive on the Deployment of alternative fuels infrastructure[3].

The work on data collection has already started while the economic analysis will start at the beginning of 2020 and the assessment's publication is expected at the same time as a possible legislative proposal.

In view of the economic analysis, both a general equilibrium model and a microsimulation model will be applied in order to study the macroeconomic impact as well as the impact on households of the proposed options. Where needed, the sectoral impact will be studied by means of appropriate quantitative tools, such as modelling already developed by the dedicated Commission services.

Evidence base and data collection [max 10 lines]

As mentioned in the Evaluation, additional data and information is needed for the assessments and analyses underpinning this initiative. In particular, in order to have a clear idea of the functioning of the Directive, effective tax rates have to be computed. An "ad hoc" questionnaire has been sent to MS in order to improve information on the volume of products covered by the different exemptions and reductions to complement the already available information on rates in the Tax in Europe Data Base[4] database.

Moreover, the OECD database on effective carbon tax rates (with the opportune countries and products adjustments) can be a valuable source of data.

Consultation of citizens and stakeholders [max 10 lines]

In addition to taking into account the results of relevant previous studies and consultations of stakeholders (on the ETD evaluation), the Commission will consult citizens and other stakeholders through a dedicated public consultation that will be launched in Spring 2020. The consultation will be based on a questionnaire, which will run for a minimum period of 12 weeks and will be made accessible via the Commission's central public consultations page (https://ec.europa.eu/info/consultations_en).

In addition, at least one stakeholders meeting will also be organised to deliver a presentation of the main issues and options under consideration and gather comments.

The main expected stakeholder groups to be consulted are:

[3] Directive 2014/94/EU of the European Parliament and of the Council of 22 October 2014

[4] https://ec.europa.eu/taxation_customs/economic-analysis-taxation/taxes-europe-database-tedb_en

Member States / public authorities Citizens (individuals) Non-governmental / civil society organisations Workers associations / trade unions Business associations Consultancies, think tanks, research / academic institutions
Will an Implementation plan be established? [max 5 lines]
An implementation plan will be prepared together with the legislative proposal.