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FICHE 6
CARBON / CO_2 TAX BASED OWN RESOURCE

1. CONTEXT

While energy taxes already exist in all EU Member States, and are harmonised to a certain degree at EU level, carbon (also called CO_2) taxes are less common. As regards energy taxes, the current Energy Taxation Directive (ETD), adopted in 2003, was designed primarily to avoid competitive distortions in the energy sector within the Internal Market. It sets out common rules on what should be taxed, when and what exemptions are allowed. Minimum rates, based mainly on the volume of energy consumed, are laid down for products used in heating, electricity and motor fuels. Above these minimum rates, Member States are free to set their own national rates.

A number of Member States have introduced specific carbon / CO_2 taxes but the majority of environment related taxes, with implications for greenhouse gas emissions, are levied on energy products and motor vehicles, rather than on CO_2 emissions directly. Currently, Denmark, Ireland, Finland, Sweden, France and Slovenia have a carbon tax in place. However, national rates are fixed at very different levels and do not reflect the carbon price under the EU ETS. Carbon taxes are usually designed to complement the ETS by taxing sectors not covered by the permit scheme.

The adoption of a carbon / CO_2 tax at the EU level would allow Member States to meet their effort sharing targets, without fear of jeopardising their competitiveness within the EU and vis-à-vis third countries. They would also prevent non-harmonised national policies from creating distortions in the Internal Market, such as double taxation situations and high compliance costs for businesses operating cross-border. Studies have shown that a carbon / CO_2 tax could also contribute to economic growth if implemented through a 'tax shift' from existing tax options which are more detrimental at macro-economic level[1].

In the Commission latest proposal to revise the ETD (2011), it was foreseen to apply a single minimum rate for CO_2 emissions (20 € per ton CO_2) to all sectors not covered by the EU ETS. This would have 'carbon priced' these sectors of the economy, namely households, transport, smaller businesses and agriculture that are outside the EU ETS. After three years of negotiations, the latest compromise text failed to address any of the main issues targeted by the Commission proposal. The proposal was therefore officially withdrawn on 7 March 2015.

2. ASSESSMENT IN RELATION WITH THE CRITERIA IDENTIFIED BY THE GROUP

1. Equity/Fairness: the current EU Energy Taxation Framework does not prevent that certain fossil fuels are taxed more favourably than cleaner competitors (e.g. exemptions on fuel used by certain sectors (agriculture); tax based on fuel volume and not on CO_2 emissions). This creates unfair competition between fuel sources and unjustifiable tax benefits for certain types of fuel compared to others. The introduction of a carbon tax would allow Member States to apply a CO_2 tax to meet their effort sharing targets, without fear of jeopardising their competitiveness within the EU and vis-à-vis third countries, would prevent different national policies from creating obstacles and distortions in the Internal Market

[1] Vivid Economics, *Carbon taxation and fiscal consolidation: the potential of carbon pricing to reduce Europe's fiscal deficits*, report prepared for the European Climate Foundation and Green Budget Europe, May 2012

and would be applied to the sectors that are not currently covered by the EU ETS (an equitable tax burden would require that it is similar to the price of the emission permit).

However, from the point of view of own resources, a carbon tax-based own resource would be questioned by Member States, given that the CO_2 intensity of the economy differs significantly from one Member States to the other. Distributional impacts would therefore have to be addressed improving fairness and ability to pay.

2. Efficiency: the introduction of an EU-wide CO_2 would give economic actors more legal certainty and reduce compliance costs, in particular if such tax would replace the various environmental tax policies in Member States. It would also serve the EU environmental-friendly objectives of reducing CO_2 and would help to address the problem of users not facing the full (social and environmental) costs of their actions. Depending on its design, it could also play an important role on the elimination of the discrimination between EU producers on the internal and world markets. For example, a destination based carbon tax could avoid a loss in competitiveness of the EU vis-à-vis the rest of the world, but might be challenging to implement for technical and legal reasons. In any case, all approaches to tax carbon / CO_2 complementarity and/or compatibility with the ETS (scope, incentives, economic incidence) would have to be ensured in order to avoid double-taxation or contradictory objectives (as was the case with the Commission proposal in 2011, which distinguished between sectors covered by the EU ETS and those outside it).

3. Sufficiency and Stability: As is the case with any 'polluter pays'-schemes, there is an inherent trade-off between revenue generated and (desired) behavioural changes. The introduction of a carbon tax particularly aims at changing energy consumption patterns, within the more general objective of moving to a low-carbon economy. Its objective is therefore primarily the reduction of carbon usage and not the provision of a stable source of revenue, which is probably why it would have to be considered as a complement only to other sources of revenue.
In theory, stability of such tax could be improved by providing for a flexible rate, or by creating it as the residual own resource based on the carbon emission of each Member State compared to the overall EU emissions (it would replace the GNI-based own resource). Measuring tools of CO_2 emissions are already in place in Member States, which could serve as base to calculate a theoretical CO_2 emission base for each Member State (similar to the currently existing theoretical VAT base calculation). This would however entail a completely new appraisal of what is a fair financing system.

4. Transparency and Simplicity: the introduction of a CO_2 tax at European level would bring more transparency to taxation of carbon, and the related tax harmonisation between Member States would create more certainty and reduce compliance and administrative costs. It would also play a role in the avoidance of double taxation. In what concerns the EU budget, transparency and simplicity would depend on the implementation and making available rules of a carbon tax as an own resource.

5. Democratic accountability and budgetary discipline: no particular role on enhanced accountability or budgetary discipline.

6. Focus on European added value and constrain narrow self-interest: The EU strives to play a leading role in the international efforts to carry forward an effective climate regime. A common, coherent carbon pricing policy including a CO_2-taxation element at EU level would be more effective than national approaches, in terms of environmental integrity, economic efficiency as well as political impact. The introduction of a CO_2 tax could also play an important role on the recovery in economic growth due to the significant revenues that can be raised while having a smaller detrimental macro-economic impact than other tax options.

7. Subsidiarity principle and fiscal sovereignty of member states: in as far as the carbon tax would be introduced by a directive; Member States would still have to implement the directive and introduce national legislation (or adjusting existing legislation), whereby the actual levying of the tax would take place at Member State level. The directive would include minimum levels of taxation. The own resources decision (including ratification requirement) would provide the revenue sharing arrangement and the principle of transfer of such tax to the EU budget.

8. Limit political transactions costs: the introduction of a Carbon / CO_2 tax is very likely to encounter a strong hostility by the transports and fuel industries. Member States more dependent on carbon based fuels would represent also a strong opposition.

3. ADVANTAGES AND WEAKNESSES OF THE CARBON TAX-BASED OWN RESOURCE

An EU approach to CO_2 taxation would create a level playing field for industry across the EU, and make cross-border activity easier. CO_2 taxation would not be applied to renewables, providing them with a further advantage compared to the conventional fuels they are competing with. A carbon tax-based own resource would thus have a clear link between a fundamental EU policy objective and the financing of its own budget.

From the point of view of own resources, the inherent trade-off between revenue generated and (desired) behavioural changes is a weakness. If such tax achieves its objective of diminishing the consumption of carbon and CO_2 emissions, the ensuing decrease of revenue should therefore be anticipated. This is particularly relevant in view of the agreement of the European Council to reduce carbon emissions by 40% in 2030 compared to 1990, to be followed by further efforts to reach cuts equivalent to 80-95% by 2050.

4. OUTCOME OF THE NEGOTIATIONS/KNOWN POSITIONS OF STAKEHOLDERS (MS, INDUSTRY, OTHER)

The 2011 Commission proposal to revise the Energy Tax Directive aimed at modernising EU rules on energy taxation by restructuring the taxation of energy products, removing the existing imbalances and distortions, and supporting the EU environmental and energy goals. Energy would have been taxed in such a way as to reflect both CO_2 emissions and energy content. The proposal was also designed to avoid double taxation and target the sectors not covered by the EU ETS (with a single minimum rate for CO2 emissions of 20 € per ton of CO2.

In its legislative resolution on 19 April 2012[2], the European Parliament -who was consulted on the proposal- expressed overall support but notably suggested the removal of the 'proportionality principle' (equal national taxation of all energy products according to their use).

Negotiations in Council proved extremely difficult (Article 113 TFEU requires unanimity). The latest compromise text failed to tackle any of the key challenges addressed in the Commission proposal on the basis of the Presidency conclusions of the European Council in 2008 (provide an adapted framework for the taxation of renewable energies; ensure consistent treatment of energy sources within the ETD in order to provide a genuine level playing field between energy consumers independent from the energy source used; complement the EU ETS). It also reduced the level of harmonisation without providing any added value for the proper functioning of the internal market or the achievement of climate change and environmental policy goals.

At the Ecofin Council of 14 October 2014, the possibility of a substantial reform of the Energy Taxation Directive proved to be close to null, even after three years of negotiations. One of the main elements of strong opposition by a number of Member States was the introduction of a CO2 tax on energy products used as heating fuels, especially on coal, coke, natural gas, LPG and kerosene (Poland, Germany and UK), as well as the tax treatment of sustainable bio-fuels, which some Member States wanted to be taxed as fossil fuels (Germany, Poland). The latest compromise text therefore foresaw that the level of CO2 to be taxed would vary according to us, thereby reducing the level of harmonisation without contributing to added value towards the proper functioning of the internal market or the achievement of climate change and energy policy goals. The Commission decided to withdraw its proposal on 7 March 2015.

[2] Taxation of energy products and electricity * European Parliament legislative resolution of 19 April 2012 on the proposal for a Council Directive amending Directive 2003/96/EC restructuring the Community framework for the taxation of energy products and electricity (COM(2011)0169 – C7-0105/2011 – 2011/0092(CNS)), OJ C 258E, 7.9.2013, pp. 144–160.

5. ESTIMATE OF REVENUE FOR THE EU BUDGET

In previous analysis (based on certain assumption of the consumption of Petrol, Diesel and LPG), the potential revenues of an "EU Energy levy" were estimated to be around 0.15% of GNI, and – if fully made available to the EU budget - could thus cover around 15% of the EU budget.

A rough calculation of an EU CO_2 levy using a EUR 10 per ton of CO_2 (falling only on sectors not covered by the ETS) resulted in estimated potential revenue of up to 28 billion by 2020 for EU27. There is no current update of these estimates.