

**EUROGAS VIEWS ON THE GREEN PAPER ON MARKET BASED INSTRUMENTS FOR ENVIRONMENT AND RELATED POLICY PURPOSES**

Eurogas, the European organisation of the natural gas industry representing the European natural gas suppliers welcomes the Commission's initiative in launching a debate on Market-Based Instruments. Eurogas, in principle supports Market-Based Instruments (MBIs) as a potentially effective tool to address the EU objectives of environmental sustainability and climate change.

In general Eurogas:

- Supports MBIs in principle;
- Calls for a careful consideration of the existing instruments and their interaction and warns against overlapping;
- Encourages efficient monitoring of the results of MBIs;
- Draws attention to the importance of preliminary impact assessment in the case of new legislative proposals.

Eurogas supports the following initiatives of the Commission:

- Creation of an MBI Forum with participation of all stakeholders;
- Revision of the Energy Tax Directive to reflect better the energy content and the environmental impact of the various fuels. The present Energy Tax Directive discriminates against natural gas and therefore its revision is a good opportunity to reverse this situation and improve the competitiveness of the cleanest of all fossil fuels.

Eurogas considers that certain proposals need further analysis and therefore reserves its position on:

- The split of minimum Tax rates
- Environmentally harmful subsidies, where a study might be necessary beforehand

The present document presents Eurogas' position on the questions raised in the Green Paper and should be considered as Eurogas' contribution to the public consultation.

## **What are the areas and options for the further use of Market-Based Instruments at EU or national level?**

Market-Based Instruments can certainly play a role particularly in changing attitudes and to a lesser extent in shaping actions. Eurogas supports further development of MBIs as long as they clearly contribute for the better functioning of the internal market and take into account the existing instruments.

Any new initiative should not distort competition (between energy sectors and between Member States) or harm the international competitiveness of European industry. It is also important that promotion of energy efficiency remains cost-efficient, thus avoiding market distortions.

Eurogas believes the aim should be to minimise intervention in the market and ensure it is proportionate and consistent with competition/market principles and structures. Any industry schemes and arrangements should be non-discriminatory and clearly targeted on particular policy objectives. The results must be measurable, so that the efficiency and effectiveness of schemes can be assessed and any necessary modifications made. MBIs should provide short term as well as long term solutions and should avoid distortions to the market. All new initiatives should be clear and easily implemented in order to avoid misinterpretation, administrative difficulties or excessive costs.

Instruments such as clearly defined funds for energy-efficient activities, certificate schemes, higher building standards and appliance labelling are also helpful in stimulating investment by companies offering energy-efficient products and services. These instruments promote the efficient use of energy, and at the same time encourage research and development in this field.

Care must be taken in introducing new MBIs to address environmental sustainability, in order to avoid the risk of double taxation, and even triple taxation on the same energy product. Instead of introducing new instruments, a coherent mix of the existing ones might be a more appropriate way of achieving EU policy objectives.

## **Could Market-Based Instruments be used in a way that promotes competitiveness, and does not impose an undue burden on consumers, in particular citizens with a low-income, but at the same time ensures revenue for public budgets?**

While Market-Based Instruments are of value, they cannot be seen as the answer to all EU objectives, especially when some of them appear contradictory. The main objective of MBIs should be to reflect the external costs of products and services, not to raise revenues. One way to extend the use of MBIs further could be to provide tax incentives for investments promoting energy efficiency.

## **Should the EU more actively pursue taxation to further Community policy purposes (in addition to fiscal objectives)? Is this the right response to current global challenges and the fiscal needs of national budgets?**

Eurogas considers that tax systems should not be overloaded with policy goals, which can be better achieved by other means. EU taxes cannot be presented as the answer to global challenges. Transfer of technology, trade policy and bilateral partnerships can sometimes be more efficient instruments.

## **Should the EU more actively promote environmental tax reforms at national level?**

Eurogas advocates a flexible approach, and supports the principle that each Member State should be free to decide the appropriate energy mix taken into account its own potential and policy. Given the differences in national circumstances, authoritative promotion of

environmental tax reforms at national level could deepen the differences between Member States and thus contradict the current objective of harmonisation. Since the effects of environmental tax reforms are difficult to predict and have an impact on the national revenues and budgets, it is better to let Member States decide their tax reforms at national level, although Eurogas supports the role of the European Commission in setting the general direction for further environmental tax reforms. This direction should lead to the harmonisation of the tax systems within the EU beyond the assessment of a new minimum tax rate for an environmental and energy tax. The total taxation on energy products has to be taken into account.

It is important to note that some countries, which have joined the European Union more recently and have not yet adapted their legislation to the EU Energy Taxation Directive, will have to alter laws which have only just been implemented or are in the process of being put in place. For these countries, as for all members states, transparent and clear information on the changes and their implications is necessary.

In general, Eurogas considers it useful to exchange information between Member States on ways of promoting tax reforms at national level in order to prevent undesired effects on the internal market.

**How could the Commission best facilitate such reforms? Can it for example offer some kind of co-ordination process or procedure?**

Eurogas supports the idea of creating a platform for exchange of best practice at EU level, similar to the proposal of an MBI Forum. This initiative should be coordinated at EU level, wherever possible through existing bodies and structures.

**Would the establishment of the abovementioned MBI Forum be useful to stimulate exchanges of experience/best practice on Environmental Tax Reform between Member States? How could it be organised in an optimal way? How should it be composed to avoid potential overlap with existing structures?**

Eurogas supports the idea of organising a Forum as long as all stakeholders are involved. Eurogas considers the role of this Forum very important in order to develop the present documents further. In order to ensure maximum efficiency, the Forum should have a clear working programme and reporting system and allow for interdisciplinary exchange of information.

**How does the need to reduce the tax burden on labour in many Member States fit with the objective to promote innovation and to support research and development in order to shift towards a "greener" economy? How can this be achieved while at the same time respecting the budgetary neutrality?**

Eurogas considers that the reduction of the tax burden on labour should not be automatically linked with the shift to greener economy, but could be pursued in parallel.

**Would a more significant tax shift towards environmentally damaging activities be the right answer?**

Eurogas favours taxation of environmentally damaging activities and recalls that natural gas should benefit from a more advantageous tax treatment reflecting its environmental and output qualities. At this stage Eurogas considers that the reform of environmentally harmful subsidies should not be considered from the tax point of view only. Other factors, such as social and economical issues should be taken into account and therefore a deeper analysis is necessary.

**What is, in the light of national experiences, the best way to advance the process of reforming environmentally-harmful subsidies?**

Eurogas looks forward to the study on environmentally harmful subsidies and their effect, announced in the High Level Group on Competitiveness. Such a study would provide the European Commission with the necessary instruments to consider a reform of these subsidies. The use of state aid to support artificially low regulated end-user tariffs should be eliminated.

**Should the Energy Taxation Directive be reviewed to make a clearer link to the policy objectives the Directive integrates, in particular in the field of environment and energy?**

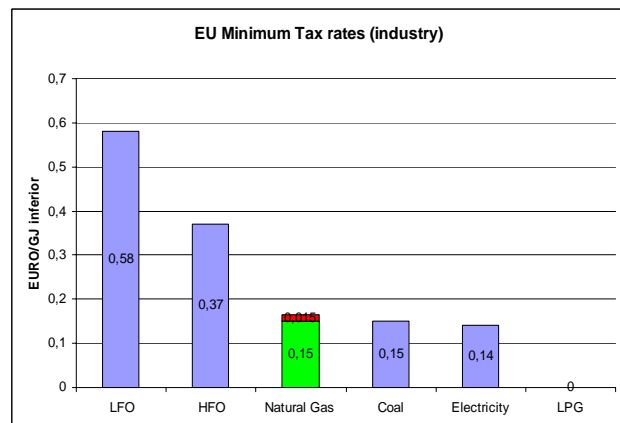
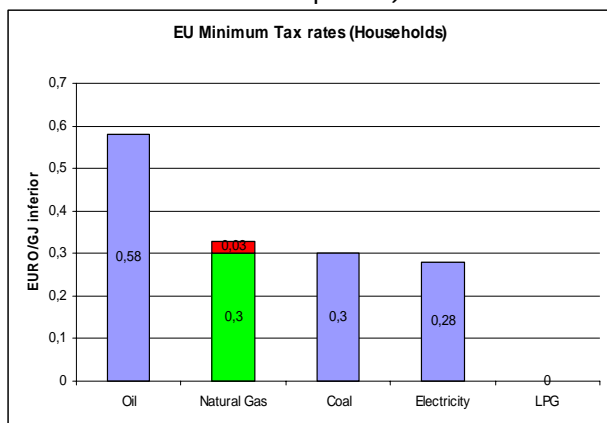
Eurogas strongly supports the revision of the Tax Directive with the objective of combining the energy and environment objectives. The main objective of such a revision should be to ensure that the principle of "polluter pays" is not jeopardised by numerous relieves, as it is the case now.

Natural gas especially if it replaces other fossil fuels will make a valuable efficient and effective contribution towards the Kyoto objectives. EU policy frameworks should be supportive of this potential.

Eurogas recalls that amongst all the fossil energies, natural gas produces the lowest CO<sub>2</sub> emissions per unit of energy. It offers important advantages in terms of greenhouse benefits (also taking into account methane releases associated with the handling and use of natural gas).

Another advantage is that, unlike with other fossil fuels, natural gas contains practically no pollutant-forming components. The exhaust of gas-fired combustion is therefore virtually free of sulphur dioxide (SO<sub>2</sub>) and particulates. Emissions of nitrogen oxides (NO<sub>x</sub>) are also low because natural gas contains hardly any organically bonded nitrogen and because combustion can occur at relatively low and constant temperatures.

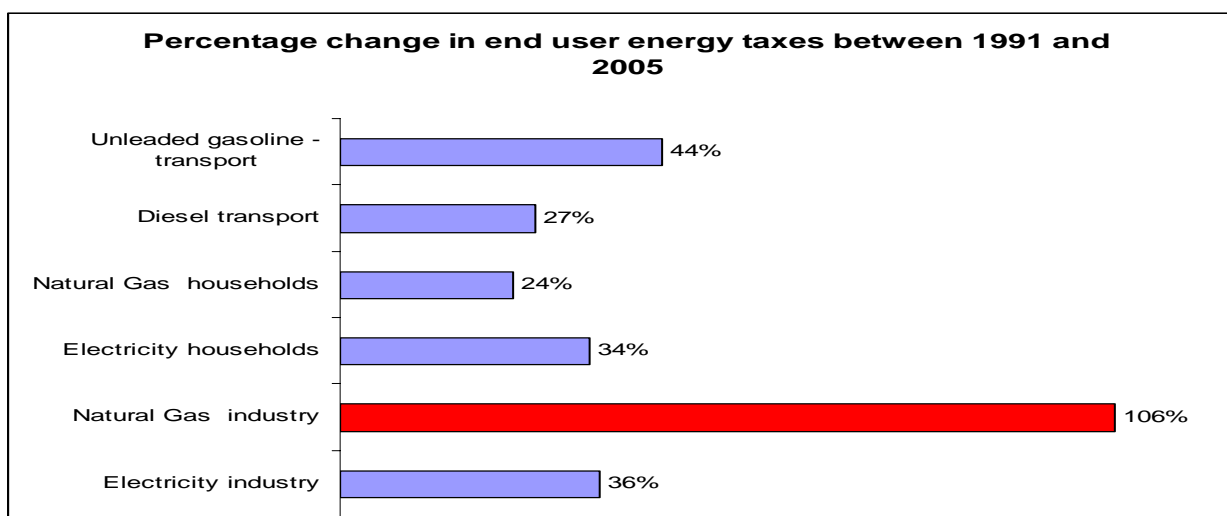
A comparison between carbon dioxide emissions and the current minimum taxation levels shows that Directive 2003/96/EC does not reflect environmental aspects. The present minimum tax levels for natural gas are even higher than the level of coal and coke in the heating market, which creates strong discrimination against the cleanest available fossil fuel, and even stronger discrimination with the zero-level for LPG. This situation favours less environmental friendly energies and does not allow the EU to reach its climate change targets. In the current exercise, Eurogas takes the opportunity to ask the Commission to correct a past mistake in the determination of the tax rates, which were calculated with different energy units (i.e. calorific values). Eurogas encourages the European Commission to treat all fuels equally, by calculating for every fuel on the basis of the Net Calorific Value (GJ inferior), thus avoiding discrimination up to 10% against the natural gas sector alone (which is currently the only fuel for which the tax rate is calculated on the basis of the Gross Calorific Value or GJ superior)



For this reason, we welcome the initiative of taking into account both the equivalent energy content and the environmental impacts of the various fuels in a weighted manner.

Eurogas also notes the importance of ensuring that the revenues generated from eventual tax corrections will be used with the clear objective of contributing to climate change objectives. Investment in new technologies should be considered.

We also warn the Commission against initiatives which raise current tax levels too much, since this could cause concern for the competitiveness of European industry and contradict the objectives of the Lisbon strategy. Referring to the natural gas sector, Eurogas notes that in the last 14 years, the taxes of natural gas for industry in EU-15 have increased much more than for other fuels, registering thus a doubling over the period. The present graph from the European Environment Agency (based on Eurostat data) clearly indicates this trend.



*Source: EN32 Energy taxes, EEA*

Before any concrete initiatives in this field are undertaken, Eurogas recalls the importance of the impact assessment study, which should analyse the eventual effect the planned tax revision will have on consumption. Another aspect to be taken into account is the proposals against the current price levels of fuels. In the last few years, the price of natural gas has seen a significant increase, which should be taken into account in working out any new initiatives. We would encourage the Commission to study carefully whether this increase has played a role in the change of consumption patterns. On the basis of such an analysis, the Commission would be in a better position to judge on the need for additional incentives and their eventual focus.

**Would this make energy taxation a more effective instrument by better combining the incentive effects of taxation with the ability to generate revenue?**

Eurogas is convinced that such a distinction will avoid market distortion and contribute towards fair treatment of the various fuels. When fixing the new rates, Eurogas wishes to encourage the European Commission to better reflect the environmental benefits of natural gas.

Applying the environmental element outside emissions trading schemes would provide an opportunity for sharing the burden of emission reduction targets. This aspect is relevant for the competitiveness of different forms of heating, as some of them are not covered by the EU ETS.

**Is splitting the minimum levels of taxation between energy and environmental counterparts the best way for doing so?**

Different systems are already in place to reflect the environmental component, such as the ETS, and so it might be more appropriate to further develop them instead of creating new instruments. Although supporting the principle of taking into account the two components (energy content and environmental impact) in a weighted manner, Eurogas is not sure that the split into two different taxes is required. In some countries this split has been effective for more than a decade, but the Paper is not explicit on how the separation of the current minimum levels of taxation into energy and environmental components would be implemented, and what rates would be applied. Eurogas supports taking into account the two components when revising the current Energy Tax Directive, but at this stage Eurogas reserves its position as far as the split is concerned due to the lack of clarity on the structure of the taxes proposed.

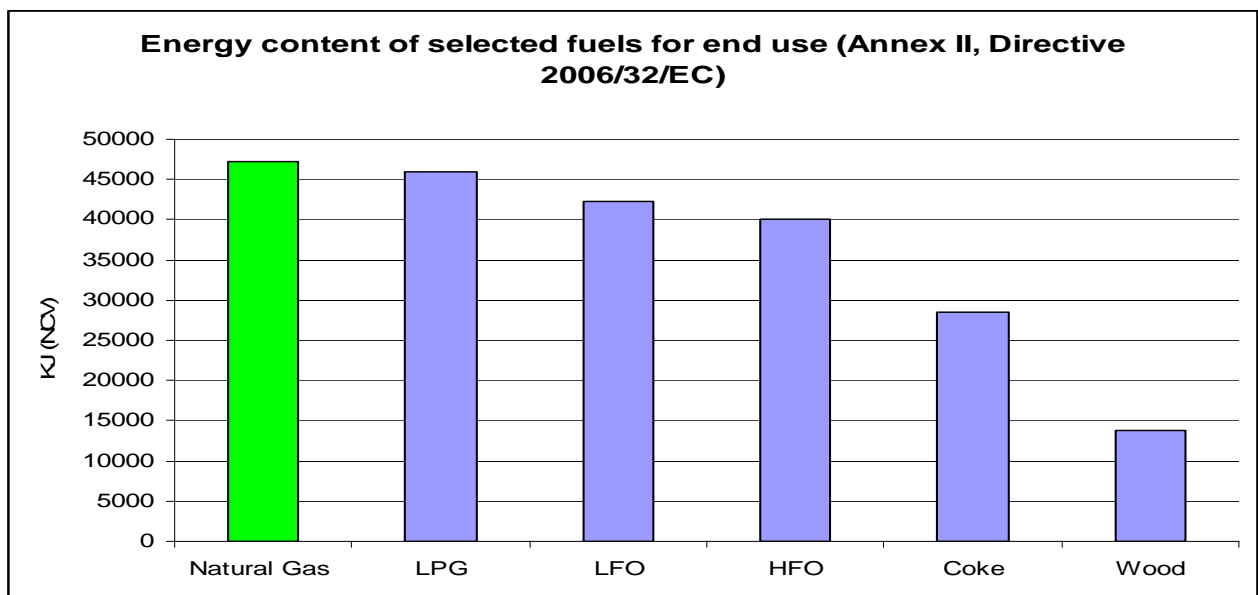
In any case, the reform of the Directive should take into account the following principles :

1) **energy content component:** the Directive should be improved by properly reflecting the energy content of the different energies. The following method is proposed :

- As for fossil fuels, this component should reflect the energy content of the different energies, to avoid distortions between them

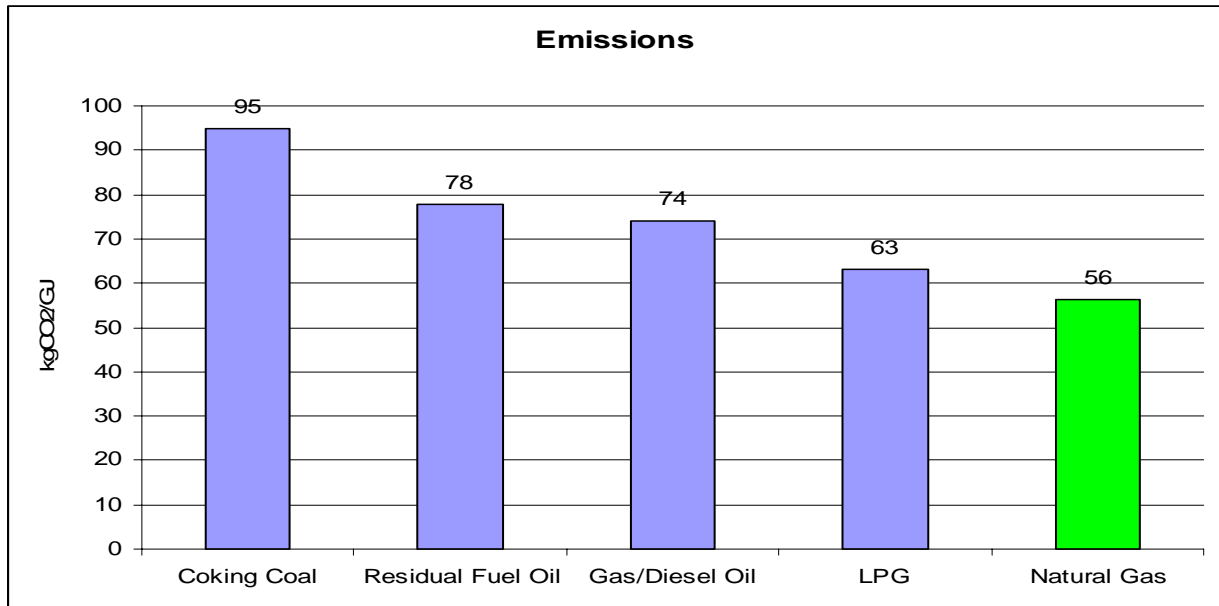
- As for electricity consumption, this component should take account of an average generation efficiency rate, thus reflecting the primary energy content at the stage of electricity generation. To avoid a double burden effect, the consumption of primary energies for generation purposes should be exempted from the energy component.

For that purpose, we recommend referring to the Annex II of Directive 2006/32/EC on energy end-use efficiency and energy services, proposing a conversion table "Energy content of selected fuels for end use ".



Source: Annex II, Directive 2006/32/EC

2) As to the **environmental component**, Eurogas considers that it should take into account all the fundamental environmental aspects such as emissions of CO<sub>2</sub>, and of other gases, as well as the production of waste.



*Source: Revised 1996 IPCC Guidelines for National Greenhouse Gas Inventories*

Referring to the proposal in the Green Paper to increase differentiation according to fuel use, Eurogas members note that in most of their countries the trend is in the opposite direction. Eurogas believes this proposal must be further developed, taking into account the current situations in EU Member States. From an industry point of view, Eurogas supports the opportunity to differentiate the dimension of energy component according to use, as for example between heating and transportation.

**What would be the pros and cons and the main practical aspects of such an approach?**

The lack of a clear view on separation and the efforts needed to determine the components and structure of the two new taxes (especially for the environmental tax), might lead to further delays in reforming the current system and to numerous complications which might obscure the primary objective of reaching the environmental goals set by the EU.

**Would the environmental incentive created by energy taxation be a sufficient and adequate response to reflect the objectives of the energy policy in the field of biofuels, including the creation of a market-based incentive for second generation biofuels?**

Eurogas accepts that, within the overall aim of CO<sub>2</sub> reduction, it may be appropriate to have short-term measures that support the development of renewables. However, once the new technologies are established and the market value of carbon is more predictable, Eurogas believes the energy mix should be primarily determined by the market, rather than by specific or binding targets. Such targets introduce distortions to the market, particularly when they overlap with other carbon reduction mechanisms. Eurogas therefore believes that as far as possible any interim support schemes should be harmonised and converge to a fully consistent and market-based EU-wide approach.

Eurogas believes that biogas has a ready role in the provision of energy from renewable sources, not least because of the possibility that this can be effectively distributed via pipeline gas systems.

**Is there a need for additional taxation addressing the remaining environmental aspects of electricity production (if any)?**

With regard to electricity production, Eurogas considers that this a complex issue. Eurogas notes that the electricity sector is already covered by regulation (e.g. emission limits for acid pollutants or binding targets for renewables) and the EU-ETS, and the remaining environmental aspects need not, in principle, be covered by an additional tax system.

Eurogas reiterates that the environmental impact of the fuel is an important criterion to be taken into account in the policy, in order to value the environmental credentials of natural gas.

**Is the proposed approach sufficient to favour uptake of electricity of renewable origin? What is the impact of such a Community framework for electricity of nuclear origin (bearing in mind the differing approaches at national level towards the use of nuclear energy)?**

The development of renewables should indeed be supported during a transitional period. The EU-ETS is the major economic and market based instrument which indirectly supports the development of carbon free power generation technologies, in particular renewables. As the impact of this instrument is not yet sufficient to make renewables economically viable, a complementary incentive is necessary during a transitional period in order to enhance their development and competitiveness. Eurogas is in favour of a harmonised and integrated approach at European level, and considers that a binding target at EU level coupled with the use of tradable certificates across Europe would be the most cost effective approach. This instrument is market based and doesn't distort competition between technologies and operators.

**Would the suggested changes to the Energy Taxation Directive and the proposed approach to its scope be the best solution for ensuring coherence between the Directive and EU ETS? Are there other options to achieve this objective?**

The primary method of ensuring greenhouse gas reductions should be to optimise the use of EU ETS by harmonising the allocation methodology and criteria at EU level, by including additional sectors of the economy and, over time, including smaller users and installations. As climate change is a global problem, the approach should also be global and other continents should be associated, in order to minimise the cost and not to harm the competitiveness of the European industry.

Eurogas supports the exclusion of the sectors covered by the EU-ETS from the scope of the environmental element of the Energy Taxation Directive as proposed in the Green Paper. Since both instruments aim for energy efficiency, the two instruments should be used in a complementary way, avoiding possible overlapping (or double burden) which could result in distortions in the market.

**What are the potential options that should be explored in order to provide the necessary incentives to encourage the EU's trading partners to undertake effective measures to abate greenhouse gas emissions?**

Eurogas fully supports the EU Emissions Trading Scheme as the key part of the EU's strategy for reducing emissions from industry and other sectors. Business needs a stable and predictable EU ETS framework to underpin the long-term value of carbon. The success

of the ETS is critical, and building the price of carbon into the power price provides support for all low carbon technologies.

An urgent priority is to set out the future objectives and design approach for the ETS post 2012. The aim should be a harmonised European allocation in emissions trading and to lay down rules for allocation from 2012 to at least 2020 to bring about long-term security. Eurogas sees this including linkages to carbon reduction schemes outside the EU, with the aim of moving progressively towards a global value for carbon.

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