## eFUEL ALLIANCE – POSITION PAPER
## REVISION OF THE ENERGY TAXATION DIRECTIVE

The eFuel Alliance welcomes the European Commission's plan to review the Energy Taxation Directive (ETD) and to present a revised version of it in mid-2021. Such a revision is well-needed as the EU's climate goals and regulations as well as energy markets and technologies have developed significantly since the current directive's adoption in 2003. The review of the ETD also offers the opportunity to take a harmonised approach when it comes to the application of tax rates to avoid distortion or fragmentation across the EU.

### RECOMMENDATIONS

→ **In order to align the ETD with the goals of the Paris Climate Agreement and the EU's policy objectives laid down in the European Green Deal, an energy taxation system that is related to climate mitigation should be introduced.**

→ **The climate performance and the positive contribution different energy sources can make to $CO_2$ reduction across different sectors, in particular in hard-to-abate areas such as the transport sector, need to be reflected.**

→ **This would set an immediate and easy-to-implement incentive for investments in the development and deployment of sustainable renewable fuels and should cover all sustainable fuels that are compatible with the Renewable Energy Directive (REDII) and the sustainability criteria defined therein.**

→ **A switch to a $CO_2$ based ETD corresponds to a $CO_2$ price of up to 300 Euros per tonne and does not entail higher costs for the end consumer if the current tax rates and the sector-specific flexibility will be maintained. Thus, supporting a socially just transition to renewable and low-carbon fuels in line with the European climate protection goals.**

### CURRENT ENERGY TAXATION DOES NOT INCENTIVISE INVESTMENTS IN LOW CARBON TECHNOLOGIES

**As pointed out in the Commission's Inception Impact Assessment, the current ETD does not adequately promote renewable fuels, such as eFuels and sustainable biofuels, nor does it provide sufficient incentives for investments in climate protection technologies.**

This is mainly due to the fact that the current taxation scheme is based on a volume-based taxation of energy products, with no direct link to the carbon content of these products, and therefore with no direct link to their climate protection potential. In the transport sector, e.g., fuels are being taxed irrespective of the $CO_2$ emissions related to the use of the product (i.e. combustion in an internal combustion engine). Hence, conventional fuels are taxed in the same way as alternative sustainable

fuels, providing no signal whatsoever to fuels suppliers or customers to supply or purchase climate friendly fuels.

The European Commission had already proposed changes to the European energy taxation in 2011[1] to better reflect the $CO_2$ footprint of an energy source. Unfortunately, the proposal had not received the necessary unanimous support from all Member States in Council. However, the climate policy and ambitions in many European countries have changed dramatically since. For the European Green Deal to be successful, energy taxation must incentivise investments in low carbon technologies. We therefore encourage the Commission to present an energy taxation system that is based on genuine criteria to reduce $CO_2$ emissions within its "Fit-for-55" legislation package.

**However, a distinction between conventional and sustainable fuels is paramount to achieving a steering effect and to incentivise the large-scale production of these environmentally preferred fuels.** Low carbon fuels still lack cost competitiveness with conventional fuels. By introducing a tax system that aims at climate protection, this cost gap could be reduced significantly, which would accelerate the process of sustainable fuels becoming competitive and set an immediate incentive for investments.

In Germany, e.g., one litre gasoline is taxed at 65 Cents, which corresponds to a $CO_2$ price of 276 euros per tonne of carbon dioxide. Adding the newly introduced cost of 25 Euros per tonne of $CO_2$ of the national emission trading system, the $CO_2$ price would be around 300 Euros per tonne and increase to around 330 Euros by 2025. Although this CO2 price would be much higher than foreseen in national legislation, this would currently not affect the cost per litre for the end consumer, offering new possibilities of shifting the market share in favour of environmentally preferred fuels.[2] This also means that a consistent consideration of the $CO_2$ footprint within the energy taxation would be more effective than an isolated integration of the transport sector in the European trading system (EU-ETS), which currently has a $CO_2$ price of around 50 Euros per tonne. Sweden, for example, as one of the most successful countries in reaching their climate goals, has achieved an impressive share of renewable energy in the transport sector, also due to an integrated $CO_2$ price in the energy taxation.[3]

## CARBON BASED TAXATION NEEDED TO REFLECT CLIMATE BENEFITS

**Instead of applying a volume-based taxation, a tax based on the $CO_2$ footprint of energy products according to REDII should be introduced, which would reflect the actual emission reduction contribution of renewable and low-carbon fuels**.[4] To reflect the actual $CO_2$ saving potential of fuels, the $CO_2$ footprint of a taxed product needs to be assessed on a lifecycle-basis, ideally taking into account all $CO_2$ emissions along the value chain.

[1] https://ec.europa.eu/taxation_customs/sites/taxation/files/docs/body/com_2011_168_en.pdf
[2] https://www.mwv.de/wp-content/uploads/2021/01/210112-Website-Position-Von-der-Energiesteuer-zum-CO2-Preis.pdf
[3] Already today, some Member States make use of a CO2-based energy taxation, e.g., Finland, Sweden, and France. These models should be assessed also with respect to social impacts and could function as starting point for discussion. See also: https://www.iwkoeln.de/fileadmin/user_upload/Studien/policy_papers/PDF/2019/IW-Policy-Paper_2019_Verkehr_Schweden.pdf
[4] In their recent study 'Energiesteuer 2.0: Konzept für eine Reform der Energiesteuer im Dienst des Klimaschutzes – Eine Steuer auf Basis von fossilem CO2' (March 2021), Frontier Economic and the FiFo Institute for Public Economics at the University of Cologne offer a concept for a reform of the energy taxation. We invite the European Institutions to carefully assess the study and incorporate its findings into the considerations when redesigning energy taxation.

The minimum tax level should consider the actual $CO_2$ footprint of the specific energy carrier. “Full” taxes arise if the fuel consists of 100% fossil origin. For the purposes of the calculation, the fossil fuel comparator laid down in Annex VI Number 19 of REDII, 94 g $CO_2$eq/MJ, should be applied. If renewable fuels are brought into market by fuel suppliers, the $CO_2$ footprint of the REDII should be considered accordingly. The energy tax should be reduced in the same proportion that $CO_2$ emissions are reduced in relation to the fossil fuel comparator.

If fuels were to be taxed based on their respective $CO_2$ footprint, this would invariably lead to a reduction of the tax burden on eFuels and sustainable biofuels, taking into account their positive climate effect. Thus, a change of the basis for taxation also provides a strong and clear signal to the market that sustainable renewable fuels shall be deployed on a large scale as quickly as possible.

The tax calculation base should always refer to the $CO_2$ footprint and should not vary depending on the sector of use. If the currently applied differentiation in tax rates for fuels depending on the respective use case or sector will be uphold, the basis for calculation should nevertheless be the same.

**In addition to an indispensable change of the basis for calculation, the revised directive should allow for an exemption for renewable and therefore environmentally preferred fuels from any minimum tax rates, giving Member States the possibility to further promote the development and use of renewable sustainable fuels as an alternative to fossil fuels.**

## CONSIDERING CONSUMER AND INDUSTRY NEEDS WHEN REDISIGNING ETD

Zero or very low taxes for environmentally preferred fuels facilitate fuel pricing that is socially acceptable, and supportive of business cases for investments. A switch to a carbon-based taxation scheme would not lead to higher costs for consumers since the tax level could remain on its current level. On the supplier/producer side however, the new tax scheme would immediately lead to strong incentives for investments in lower carbon fuels.

The energy tax constitutes an important source of income for most EU Member States. According to the final report on energy taxes, the revenues from taxes on energy consumption in the EU27 amounted to 263 billion Euros in 2018.[5] Once larger volumes of renewable fuels will be introduced to the market, Member States’ tax revenues would decrease due to the decrease in the use of fossil fuels. This could be compensated by a collateral increase of the tax rate for fossil fuels to guarantee constant income for Member States and to incentivise the development of innovative fuels.

However, it is the EU’s goal to decarbonise and defossilise our economy, which will inevitably lead to a reduction in the use of fossil energy carriers. In the transport sector, other policy measures such as the expansion of e-mobility or a switch to other means of transport such as rail transport will have similar effects on Member States’ tax revenues. With a view to the EU’s ambitious climate goals and the undisputable necessity to defossilise our economy, a long-term reorientation of state financing should be considered.

[5] https://op.europa.eu/en/publication-detail/-/publication/39fa0090-1750-11eb-b57e-01aa75ed71a1/language-en

**Given that the energy taxation constitutes an excise duty, an indirect consumer tax, social considerations and consumer acceptance are important and need to be considered when redesigning the energy tax**. If only the basis for calculation is changed, there will be no immediate impact on the costs for consumers or the industry. The possibility of defining separate tax rates for specific sectors constitutes one of the main socio-political advantages of the energy taxation in comparison to the European trading system (EU-ETS), as a higher taxation of transport would not impair other sectors like heating, making the energy transition more just and socially acceptable. Potential long-term impacts as a result of additional changes could be mitigated through additional social or economic policy measures.

With increased quantities of eFuels being added gradually to conventional fossil fuels, and production costs falling due to economies of scale, eFuels would be affordable from the very beginning of this process for consumers as well as for hard-to-abate sectors like aviation and maritime. Renewable fuels are therefore a cost-effective and economic $CO_2$ reduction option that can increase consumer acceptance.[6]

## HOLISTIC POLICY FRAMEWORK TO ENABLE MARKET RAMP-UP

**When revising the ETD, alignment of the directive with other EU climate regulation is inevitable. In particular, it needs to be in line with the REDII. Sustainability criteria applied in the ETD should be based on the criteria laid down in REDII. The overhaul of the current energy tax system constitutes an important step on the way towards climate neutrality.** In combination with other crucial regulatory measures to promote the widespread use of sustainable fuels – such as an ambitions revision of REDII, incl. a minimum quota of 5% for renewable fuels of non-biological origin (RFNBOs), such as eFuels and hydrogen; or the introduction of a crediting mechanism for renewable fuels within the revision of the $CO_2$ emission standards – incentives for investments in clean fuel technologies will be set and a market ramp-up of these fuels can be achieved.

As a $CO_2$-neutral alternative to conventional fossil energy carriers, sustainable renewable fuels can make a decisive contribution to the global energy transition. A wide use of these fuels will have a positive effect on costs for all use-cases and sectors as well as for end users in all EU Member States. To accelerate the decarbonisation and defossilisation of Europe, a multi-solution approach should be applied, supporting the deployment of different climate protection solutions.

### ABOUT THE eFUEL ALLIANCE

The eFuel Alliance is a stakeholder initiative committed to promoting the political and social acceptance of eFuels and to securing their regulatory approval. We represent more than 130 companies and associations along the value chain of eFuel production. We stand for fair competition and a level-playing field for all relevant emission reduction solutions. We are clearly committed to more climate protection and aim to win broader recognition of the significant contribution eFuels can make in the drive for sustainability and climate protection. Our goal is to facilitate the industrial production and widespread use of carbon neutral fuels made from renewable energy sources.

[6] For production cost and price development at the filling station, see for example: Prognos et al. 2018: Status And Perspectives Of Liquid Energy Sources In The Energy Transition