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**Including consumption in the EU ETS –
Administrative implementation of a
consumption based charge**

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A blueprint for the Inclusion of Consumption in the EU ETS

The “Inclusion of Consumption in EU ETS” is currently gaining traction as a new approach to address carbon leakage and improve the effectiveness of the EU ETS, within legal and political constraints. It complements the current approach of coverage of emissions by upstream installations where trade exposed sectors at risk of leakage, such as steel and clinker, receive free allowances. In order to ensure the recovery of carbon costs from consumers, we propose the introduction of a complementing second pillar. This would be facilitated by adding a consumption-based charge to the EU ETS directive (the Charge). The Charge would be based on the EU ETS permit price and the benchmark employed for the allocation of free allowances. It would be levied when carbon intensive goods are released for consumption. Funds raised would be assigned to national trusts, which would be strictly separated from the national budget.

This report provides a blue print for the administration and control of the “Inclusion of Consumption”. The proposed approach builds from the administration of other consumption based levies including excise and Value Added Tax (VAT). The research has been informed via a literature review, case studies with businesses that produce excisable goods as well as interviews with public authorities, academics and excise administration experts. Importantly, the intent is not to design an all-encompassing administrative framework, but rather to demonstrate how such a system may function. The critical elements of the approach are outlined below and expanded on in the course of the report.

Scope

- **Coverage** - The “Inclusion of Consumption” should cover specific carbon intensive commodities like steel or clinker (for cement).
- **Liability creation** - Carbon liabilities would be created with the production (e.g. hot rolled steel, clinker) or importation of products from these sectors. However, the charge would become due only when the product is released for consumption, i.e. leaves the Production Sphere and enters the Consumption Sphere.
- **Calculating the charge** - The charge would be calculated according to the weight of the carbon intensive good, pre-existing European Best Available Technology (BAT) benchmarks and the average EU ETS permit price for the last quarter prior to release for consumption.
- **The Production Sphere** - Registered entities producing, handling, and manufacturing covered products can do so charge free under duty suspension arrangements within the Production Sphere.
- **The Consumption Sphere**- a product enters the Consumption Sphere when it is exported, sold or transferred to an unregistered entity or to a final consumer. In addition, any carbon intensive products used as production equipment or wasted in the production process are considered to have entered the Consumption Sphere, thus triggering carbon duties.
- **De minimis** - thresholds should apply to imports with a small carbon value to product value ratio. Such thresholds are to be implemented through the ProdCom list. Product categories that do not exceed the threshold are exempt from the scheme. The list should be revised in five year periods in parallel with the Carbon Leakage List.

Licensing and registration

Duty suspension requires those entities dealing in the production, transportation and storage of goods to be licensed. Licenses for Carbon Keepers should be granted on the following conditions:

- *adoption of minimum accounting standards;*
- *records of stock and movement of duty suspended carbon intensive products;*
- *compliance with other fiscal obligations (direct taxation, customs, VAT);*
- *compliance with the requirements laid down by the Member State within whose territory an entity is situated;*
- *notification of changes to business activities or structure; and*
- *provision of guarantees, where required to eliminate substantial financial risks.*

Licenses for Carbon Warehouses should be granted on the following conditions:

- *details of the address and a description of the premises are provided;*
- *details of the stock reporting system are provided; and*
- *records, for each Carbon Warehouse of stock and movement of carbon intensive products are kept.*

Monitoring, reporting and verification

A system for monitoring, reporting and verification is to be established which provides assurance that the amount of liability paid and held under suspension arrangement reflects the level of liability created in the overall system. Such a system should include:

- **Electronic reporting** - *A Carbon Monitoring and Control System (CMCS) be established to track the movement of duty suspended carbon intensive goods.*
- **Reporting** - *all Warehouse Keepers must report (in weight) production volumes, in going and outgoing movements and the level of storage of carbon intensive goods into the CMCS.*
- **Adjustments** - *exports and products moved to another registered entity should be deducted from a registered entities liability.*
- **Write offs** - *there shall be no write-offs for products lost, wasted, or damaged during the production process.*
- **Acquittal** - *at the end of the reporting period, all warehouse keepers must pay their liability calculated from the CMCS.*
- **Simplified reporting** - *procedures could be considered for trade within a Member State, regular bilateral trade between Member States, and movement between warehouses registered to the same warehouse keeper.*

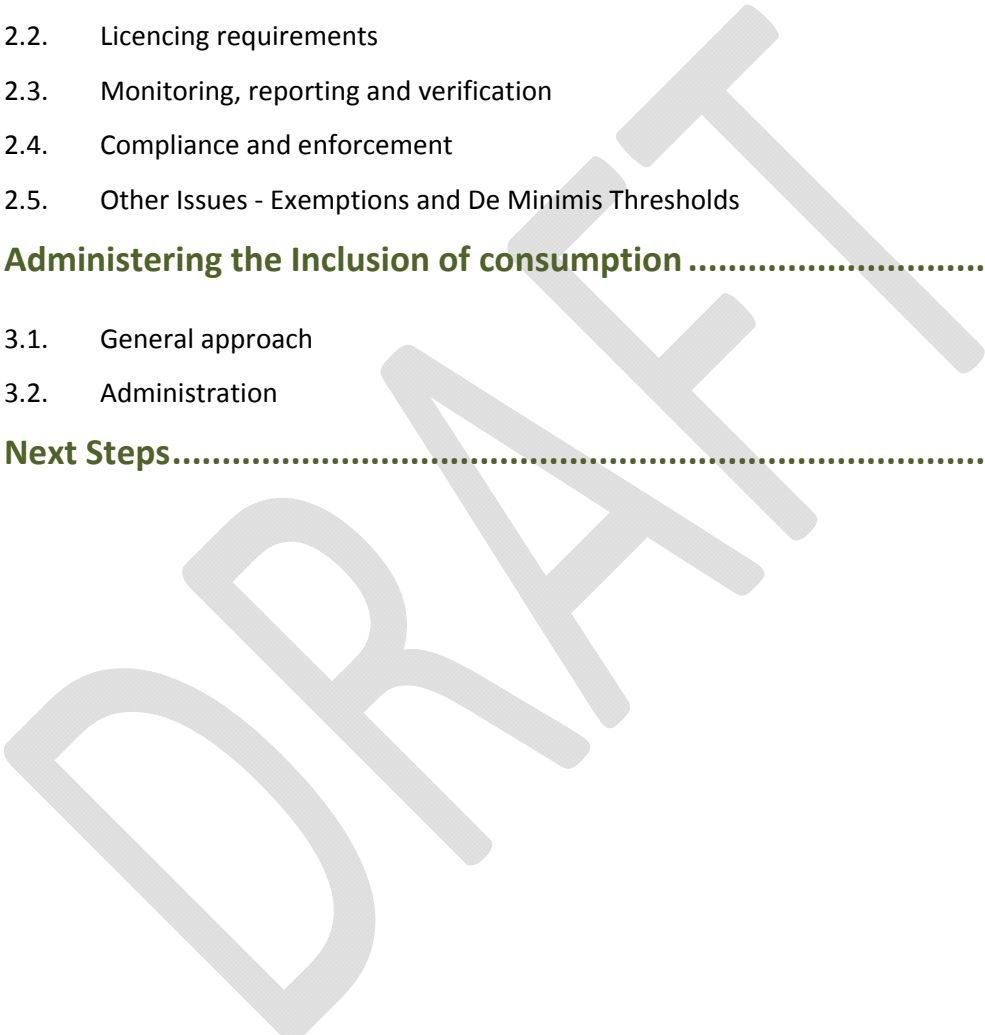
Compliance and enforcement

The following enforcement mechanisms are recommended:

- *Relevant agencies carry out enforcement actions including audits, unannounced site visits and stock takes.*
- *Anti-abuse laws should be drafted to limit criminal abuse of the scheme.*
- *Imports and exports of metal declared as scrap should be monitored across European Union external borders.*

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1. INTRODUCTION

In a world of uneven climate policies, carbon pricing within the European Union raises concerns regarding carbon leakage and the competitiveness of carbon intensive and trade exposed industries.¹ European producers in these industries compete in a global market with firms facing lower or no carbon pricing.

Within the carbon leakage debate, both carbon border adjustments (also referred to as border levelling) and consumption taxes on embedded emissions (carbon taxation) have received significant attention². In the case of border levelling, full auctioning under the European Union Emission Trading System (EU ETS) would be supported by a charge equivalent to the Best Available Technology (BAT) on both exports and imports. Leakage would then be avoided and the carbon price signal would remain intact, creating incentives for innovation in new production processes and products. Although economically sound, political and legal constraints have hindered the implementation of border tax adjustments thus far. Politically, it is thought that border levelling needs to be embedded in formal or informal international cooperation to contribute to trust between countries, affecting prospects for a future international agreement. Legally, the compatibility of border tax adjustments with world trade law is still controversial.

In the case of a consumption tax on embedded emissions, a tax would be levied on products purchased by European consumers, irrespective of the origin of the product. From an economic perspective, a consumption tax would ensure incentives for carbon mitigation and efficient consumption. However, the Treaty on the Functioning of the European Union³ makes the adoption of environmental taxes difficult as ‘provisions primarily of a fiscal nature’ require a unanimous decision in the European Council (Article 192 para 2 lit. a TFEU). This voting ratio, which in the 1990s has led to the failure of the proposal for a carbon tax, means that a consumption tax on embedded emissions may be considered politically infeasible.

Given these legal and political constraints, “the Inclusion of Consumption in the EU ETS”⁴ has emerged as a new approach to address carbon leakage and improve the effectiveness of the EU ETS. It complements the current approach of coverage of emissions by upstream installations where trade exposed sectors at risk of leakage such as steel and clinker receive free allowances. In order to ensure the recovery of carbon costs from consumers, we propose the introduction of a complementing second pillar. This would be facilitated by adding a consumption-based charge to the EU ETS directive (the “Charge”). The Charge would be based on the EU ETS permit price and the

¹ According to the ETS Directive (Article 10a), a sector or sub-sector is deemed to be exposed to a significant risk of carbon leakage if the extent to which the sum of direct and indirect additional costs induced by the implementation of the directive would lead to an increase of production cost, calculated as a proportion of the Gross Value Added, of at least 5%; and the trade intensity (imports and exports) of the sector with countries outside the EU is above 10%.

² Susanne Dröge et al., Tackling Leakage in a World of Unequal Carbon Prices, Climate Strategies 2009; Roland Ismer and Karsten Neuhoff, Border tax adjustment: a feasible way to support stringent emission trading, Eur J Law Econ (2007) 24.

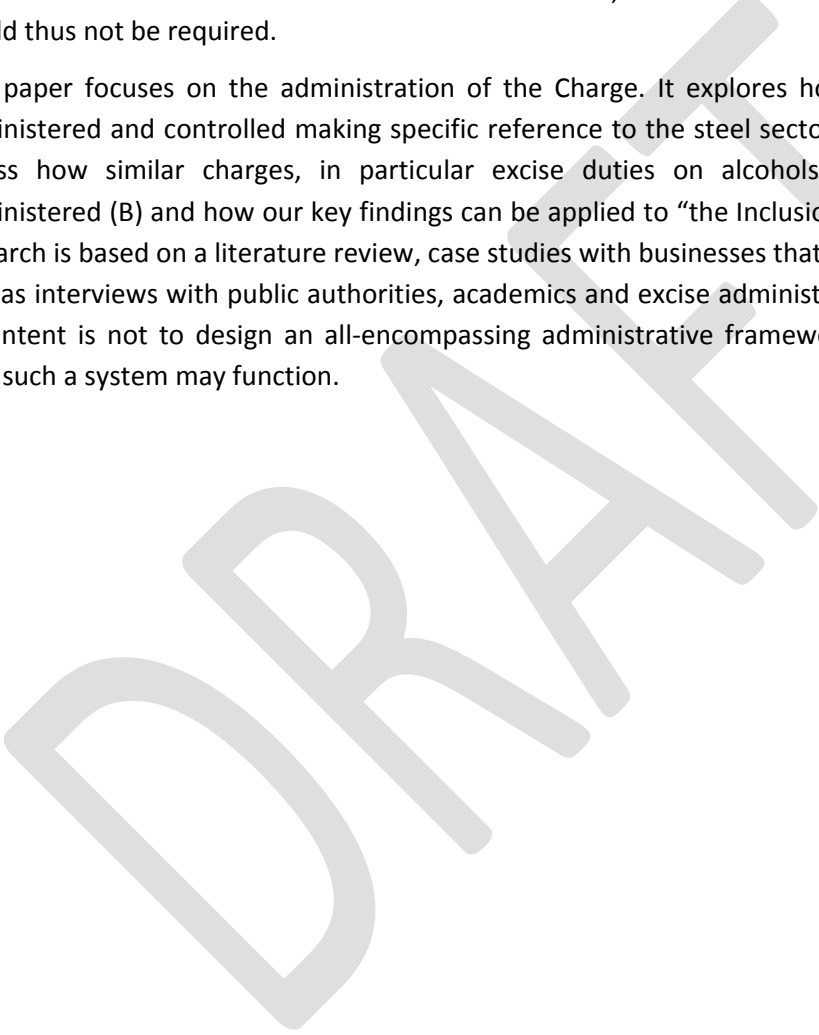
³ Treaty on the Functioning of the European Union, [2012] OJ C 326/47 (TFEU).

⁴ For further information about the inclusion of consumption, in particular the legal analysis of the scheme see Roland Ismer and Manuel Haussner, Including consumption in the EU ETS – A chance for the European Union to overcome carbon leakage (forthcoming).

benchmark employed for the allocation of free allowances. It would be levied when carbon intensive goods are released for consumption. Funds raised would be assigned to national trusts, which would be strictly separate from the national budget. The trusts would use the funds for acquiring and retiring allowances to compensate for net-imports of carbon embedded in energy intensive commodities. The remainder would be assigned to fund climate action in line with the priorities formulated for EU ETS auction revenues.

The Charge would not constitute a tax so that it could be adopted under the ordinary legislative procedure in the European Council (Article 192 para 1 TFEU). The scheme would be closely linked to the EU ETS (carbon price and benchmarks). Moreover, funds collected would not flow to Government revenue. A unanimous vote in the Council, which would be necessary for a carbon tax, would thus not be required.

This paper focuses on the administration of the Charge. It explores how such a charge could be administered and controlled making specific reference to the steel sector. To inform the design, we assess how similar charges, in particular excise duties on alcohols and tobacco, have been administered (B) and how our key findings can be applied to “the Inclusion of Consumption” (C). The research is based on a literature review, case studies with businesses that produce excisable goods as well as interviews with public authorities, academics and excise administration experts. Importantly, the intent is not to design an all-encompassing administrative framework, but rather to illustrate how such a system may function.



2. LEGAL FRAMEWORK AND EXPERIENCE WITH CONSUMPTION BASED LEVIES

Consumption levies have been implemented on a global scale.⁵ Two of the most well-known examples are Value Added Taxes (VAT) and excise duties. Whereas VAT is levied on a broad base, calculated based on the value of traded goods and imposed at each stage of the transaction⁶, excise duties are:⁷

- levied on a limited range of products;
- imposed when released for consumption; and
- calculated according to the weight, volume, strength or quantity of a product.

Given these characteristics, excise duties provide a pertinent model as to how a consumption-based charge could be administered and controlled.

In this chapter, the European excise administration and control system is assessed, in the context of what can be learnt for the administration of the Inclusion of Consumption in the EU ETS. In doing so, a high level review of the excise arrangements is provided before discussing findings from the literature and discussions with industry participants.

2.1. The functioning of the European Excise scheme - duty suspension arrangements

Within the European Union, the general arrangements for excise duties and their implementation and administration are laid out in the Council Directive 2008/118/EC.⁸ This Directive is supplemented by further directives, which establish additional rules for specific excise goods. Member States have to implement the European excise scheme through their national laws, which are based on these directives.

Administratively, the European excise scheme is governed by the Electronic Movement and Control System⁹ (EMCS) and the System for the Exchange of Excise Data (SEED). The EMCS is an electronic system for monitoring the movement of excise goods. By allowing an intra-European matching of data, the movement of excisable goods is effectively monitored. Hence the EMCS represents a strong

⁵ OECD, Consumption tax trends 2012 – VAT/GST and excise rates, trends and administration issued, p. 28.

⁶ Cf. OECD, Consumption tax trends 2012 – VAT/GST and excise rates, trends and administration issued, p. 31.

⁷ OECD, Consumption tax trends 2012 – VAT/GST and excise rates, trends and administration issued, p. 39 et seq.

⁸ Council Directive 2008/118/EC of 16 December 2008 concerning the general arrangements for excise duty and repealing Directive 92/12/EEC [2009] OJ L 9/12.

⁹ Decision No 1152/2003/EC of the European Parliament and the Council of 16 June 2003 on computerizing the movement and surveillance of excisable goods, [2003] OJ L 162/5; Commission Regulation (EC) No 684/2009 of 24 July 2009 implementing Council Directive 2008/118/EC as regards the computerized procedures for the movement of excise goods under suspension of excise duty, [2009] OJ L 197/24.

tool to limit tax evasion. The EMCS is supplemented by SEED, a national and European database which provides data of all participants in the excise scheme.

2.1.1. Scope of excise law

Within the European Union, excise duties are applicable to beer¹⁰, wine¹¹, ethyl alcohol¹², manufactured tobacco (including cigarettes, cigars, cigarillos and smoking tobacco)¹³, as well as energy products and electricity¹⁴. In general, an excise liability is created when an excise good is produced, extracted or imported into the European Union (Article 2 DIR 2008/118/EC). However, excise only becomes chargeable at the time, and in the Member State, of release for consumption (Article 7 para 1 DIR 2008/118/EC). This means that excise is not due as long as products remain within the Production Sphere and are not released for consumption.

2.1.2. Duty suspension arrangements

The distinction between the Consumption and Production Sphere is governed by duty suspension arrangements. Duty suspension arrangements are fiscal rules¹⁵ which, under certain conditions, suspend the payment of excise. As long as goods are held under such arrangements, they have not been released for consumption so that excise is not due.¹⁶ Duty suspension arrangements allow licenced (see below) entities to produce, process, hold, transport and trade excise goods between producers of different production stages without triggering excise. The duty is transferred along the supply chain until excise goods are released for consumption. When excise goods depart from suspension arrangements or are held, produced or imported outside such arrangements, they are released for consumption and duty has to be paid. The duty must be paid by the person releasing excisable goods from duty suspension arrangements (Article 8 para 1 DIR 2008/118/EEC). For this purpose, registered entities must submit a monthly return to the relevant national authorities and pay any charges due.

To ensure fiscal supervision and effective monitoring of excise goods¹⁷, duty suspension arrangements only apply to goods which are produced, processed and held within tax warehouses¹⁸ and which are moved between warehouses or other registered entities. Tax warehouses are spatially

¹⁰ See Articles 1, 2 Council Directive 92/83/EEC of 19 October 1992 on the harmonization of the structures of excise duties on alcohol and alcoholic beverages, [1992] OJ L 316/21.

¹¹ Articles 7 (1), 8 DIR 92/83/EEC.

¹² Articles 19 (1), 20 DIR 92/83/EEC.

¹³ Articles 1, 2, 3, 4, 5 Council Directive 2011/64/EU of 21 June 2011 on the structure and rates of excise duty applied to manufactured tobacco, [2011] OJ L 176/24.

¹⁴ Detailed information about energy products subject to excise tax given by Articles 1, 2 Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity, [2003] OJ L 283/51.

¹⁵ Harald Jatzke, Production, holding and movement of excise goods under duty suspension within the European Union, *World Customs Journal*, Vol 6 No 2, p. 3.

¹⁶ Harald Jatzke, Production, holding and movement of excise goods under duty suspension within the European Union, *World Customs Journal*, Vol 6 No 2, p. 4.

¹⁷ Harald Jatzke, Production, holding and movement of excise goods under duty suspension within the European Union, *World Customs Journal*, Vol 6 No 2, p. 4.

¹⁸ A tax warehouse is defined as “a place where excise goods are produced, processed, held, received or dispatched under duty suspension arrangements by an authorised warehouse keeper in the course of his business, subject to certain conditions laid down by the competent authorities of the Member State where the tax warehouse is located” (Article 4 Nr. 11 DIR 2008/118/EC).

defined areas and can comprise a certain part of premises, the whole premises or even a range of premises within a certain neighbouring region.¹⁹ In the case of the movement of excise goods, duty suspension arrangements apply if excise goods are moved between tax warehouses or between a tax warehouse and a registered consignee²⁰.

2.1.3. Imports and exports

Excise goods can also be moved under duty suspension arrangement from the place of importation to a tax warehouse (Article 17 para 1 lit. b) DIR 2008/118/EC). This, however, is only possible if goods are dispatched by a registered consignor upon their release for free circulation in accordance with Article 79 CCC (Article 4 No 10 DIR 2008/118/EC). Imported goods may also be placed under customs suspension arrangements.²¹ Such arrangements imply that excise is not due if excise goods (e.g. tobacco) are imported solely in order to be processed within the European Union. In contrast, if no duty suspension arrangement follows the release for free circulation, excise is payable by the person who declares the excise goods or on whose behalf they are declared upon importation (Article 8 para 1 lit d) DIR 2008/118/EC).

In the course of exportation, excise goods can be moved under duty suspension arrangement from a tax warehouse to the place where they leave the territory of the European Union (Article 17 para 1 lit a) iv) DIR 2008/118/EC). Thus, excise duty will not be charged. European excise legislation does not set any rules for the exportation of excise goods outside duty suspension arrangements, i.e. for excise goods on which excise duty is already imposed. Some Member States provide a reimbursement of excise duties for such exports, while others do not.²²

2.1.4. Re-entering tax warehouses

While uncommon, goods for which duty has been paid may in some circumstances re-enter tax warehouses and be placed again under duty suspension arrangements. This could occur, for example, due to incorrect deliveries, product defects, a customer seeking a return and refund or simply because trade takes place between an unregistered and a registered entity. In this case, excise duties would again be charged when the product is released for consumption. To avoid double charging, credits or a reimbursement of duties originally paid are made by some Member States.²³

¹⁹ Cf. Sec. 4 BierStG, Sec. 3 BierStV; Irish Tax and Customs, Authorisation of Warehouse keepers and Approval of Tax Warehouses Manual, 3.2.

²⁰ “a registered consignee” means a natural or legal person authorised by the competent authorities of the Member State of destination, in the course of his business and under the conditions fixed by those authorities, to receive excise goods moving under a duty suspension arrangement from another Member State;“ (Article 4 No. 9 DIR 2008/118/EEC).

²¹ Article 4 No 8 DIR 2008/118/EC; Such procedures encompass external transit, customs warehousing, inward processing in the form of a system of suspension, processing under customs control, temporary importation (Article 84 (1) lit a) CCC).

²² I.e. excise duty can be reimbursed in the UK if excise goods are not consumed within the UK and exported outside the EU (HM Revenue and Customs, Notice 2007 Excise Duty: drawback, May 2014, 3.1. No reimbursement is provided in Germany (see http://www.zoll.de/DE/Fachthemen/Steuern/Verbrauchssteuern/Alkohol-Tabakwaren-Kaffee/Steuerrechtlich-freier-Verkehr/Warenverkehr-Drittland/Ausfuhr/ausfuhr_node.html).

²³ Cf. Sec. 24 (1) BierStG (German excise regulation concerning excise tax applicable to beer products); Sec. 42 BierStV.

2.1.5. Stakeholder input

Discussions with industry experts revealed that a high value is placed on the flexibility allowed for by duty suspension arrangements. Specifically, those entities that are involved in the production but not distribution of excise goods or produce goods for the external market do not have to pay excise duties. For those entities that do participate in the excise scheme, duty suspension arrangements payment allows for the management of cash flows.

Key Learnings

Duty suspension allows a clear demarcation between the Production and Consumption Sphere.

Duty suspension arrangements allows the charge to be implemented close to the point of final consumption.²⁴

Duty suspension requires effective administration and control procedures to protect government revenues and the integrity of the scheme.

Current design of excise legislation allow the import of products for inward processing without triggering excise liability.

2.2. Licencing requirements

Liabilities are created via the production, resource extraction (for example energy products) or importation of excisable goods within the European Union. These liabilities can then be transferred through the supply chain by entities, which transform or further manufacture excisable goods. Licencing and registration is required for all types of activities that deal with excise goods under duty suspension arrangements. Licencing and registration enables national authorities to identify liabilities, control excise goods effectively and ensure that mechanisms are in place to avoid tax evasion.²⁵

²⁴ Final consumer refers to the end consumer of a product.

²⁵ Harald Jatzke, Production, holding and movement of excise goods under duty suspension within the European Union, *World Customs Journal*, Vol 6 No 2, p. 3.

2.2.1. Licensing requirements for authorised warehouse keepers

Under the European excise scheme, European legislation only lays down a limited range of requirements for the authorisation of warehouse keepers and gives Member States discretion to stipulate further conditions.²⁶ Thus, a warehouse keeper must:²⁷

- provide, if necessary, a guarantee to cover the risk inherent in the production, processing and holding of excise goods;
- comply with the requirements laid down by the Member State within whose territory the entity is situated;
- keep, for each tax warehouse accounts of stock and movement of excise goods; and
- enter in his accounts at the end of their movement all excise goods moving under duty suspension arrangement and consent to all monitoring and stock checks.

In addition, the European Commission published guidelines for the authorisation of warehouse keepers.²⁸ These guidelines are discussed in Box 2.1 below.

Box 2.1: European Commission guidelines for the authorisation of Warehouse Keepers

According to the European Commission's guidelines, the acceptance of an applicant should be based on information such as: the company's accounting system; internal control measures and methods of audit; details of the company's financial position, its revenue history and its compliance with other fiscal obligations (customs, VAT, direct taxation); the level of storage; and estimates of goods to be produced, held or moved in a given period.²⁹ If guarantees are required, the amount of guarantee should only reflect the risk inherent in the activities of the warehouse keeper or the registered trader and should be under regular review.³⁰

2.2.2. Licensing requirements for tax warehouses

Requirements for the registration of a tax warehouse are also at the discretion of the Member States (Article 16 para 1 DIR 2008/118/EC). However, it is common across Member States that authorised warehouse keepers provide the address and a description of the premises that is to be licensed as a tax warehouse, in addition to architectural drawings or plans of the premises and details of the stock reporting system.³¹ Furthermore, the European Commission recommends that national authorities, in

²⁶ Cf. Irish Tax and Customs, Authorisation of Warehouse keepers and Approval of Tax Warehouses Manual, Section 3.4.; Sec. 4, 5 BierStV; HM Revenue and Customs, Notice 196 Excise goods: registration and approval of warehouse keepers, warehouse premises, owners of goods and registered consignors, Section 3.

²⁷ See Article 16 DIR 2008/118/EC.

²⁸ Commission Recommendation of 29 November 2000 [2000/789/EC] setting out guidelines for the authorisation of warehouse keepers under Council Directive 92/12/EEC in relation to products subject to excise duty (notified under document number C(2000) 3355).

²⁹ Art. 2 (2) Commission Recommendation 2000/789/EC.

³⁰ Article 6 Commission Recommendation 2000/789/EC.

³¹ Compare Irish Revenue Notice No. 1890, March 2014, Excise – Authorisation of Warehouse keepers and Approval of Tax Warehouses; HMRC Reference: Notice 196 (October 2012), Excise goods: Authorisation of warehouse keepers and approval of premises, 4.4; Sec. 4 BierStV.

order to form a clear view of the existence and structure of the premises and the warehouse, carry out a pre-authorisation site visit.³²

2.2.3. Issuance of excise registration numbers

If all requirements are met, an individual excise registration number is issued to the authorised warehouse keeper and each tax warehouse which is operated. These individual excise registration numbers are stored in SEED, a database which is made available to all participants of the excise scheme. This allows them to gain information about the status of trade partners and check whether excise goods can be moved under duty suspension.³³

2.2.4. Stakeholder input

Industry participants noted that across most Member States, registering a tax warehouse for excise purposes does not entail substantial costs as tax warehouses must only meet low requirements (be considered a locally defined place and maintain book-keeping requirements). Nevertheless, gaining the status of an authorised warehouse keeper could be a burden for some, in particular smaller, producers. This is largely the result of lacking sufficient legal capabilities to effectively navigate the application procedure, resulting in lengthy delays or the use of (costly) professional consultants.³⁴ In addition, delays in the application process can in some instances result in costs to businesses. Industry participants suggested that better access to standardised documents as well as services such as help-desks and online tutorials could significantly reduce these administrative barriers and therefore lower costs. Furthermore, direct and timely access to staff from the relevant authorities was considered to be of great value.

Literature on excise systems as well as discussions with interview participants highlighted a number of co-benefits that may arise from licencing and registration requirements. Firstly, going through the licence application processes allows for dialogue between licence holders and the relevant authority. Such dialogue can increase trust between the public and private sector, increasing self-compliance and reducing the need for physical controls³⁵. Secondly, licencing criteria can also be used to reduce the costs of monitoring and enforcement. For example, requirements regarding how products should be stored can reduce the costs of physical audits, if and when they become necessary.

Key Learnings

Registration and licencing are a systemic necessity to assure the effective control of consumption charges. However, the requirements, which have to be met for registration purposes, should not be overly onerous. As a general rule, striking this balance requires stricter licencing requirements for those entities which produce or manage larger liabilities.

Access to assistance in completing the registration process, either through online forms, help desks, tutorials etc., can reduce the administrative cost of licencing for smaller businesses.

³² Article 3 Commission Recommendation 2000/789/EC.

³³ Harald Jatzke, Production, holding and movement of excise goods under duty suspension within the European Union, *World Customs Journal*, Vol 6 No 2, 5.

³⁴ Some interview participants noticed that this was not a concern unique to excise administration.

³⁵ World Health Organisation, WHO Technical Manual on Tobacco Tax Administration, Report Number ISBN 978 92 4 156399 4 (2011).

2.3. Monitoring, reporting and verification

The aim of reporting is to ensure that the liabilities which have been created, sit correctly in licensee's records. This requires tracing the liability as it moves through registered participants at each stage of the supply chain. Liabilities stemming from production, importation or the sale of final products can be monitored relatively easily and reconciled through reference to standard business records or transactions conducted with the relevant customs authority³⁶. However, monitoring and reporting on liabilities as they move through the manufacturing stage can be a little more complex. The processes for monitoring and reporting under the European excise scheme are discussed below.

2.3.1. Monitoring the movement of excisable goods

Movement of excisable goods is monitored through the EMCS, an electronic procedure that allows tracking and tracing of excise goods under duty suspension.³⁷ If a consignor wishes to dispatch excise goods under duty suspension, they must submit an electronic administrative document (e-AD), which is validated by the Member State in which the dispatch took place. The validation mainly encompasses a matching of the excise numbers of the consignor and the consignee against SEED. Assuming no discrepancies, the e-AD is sent back to the consignor who then hands over a copy to the carrier. At the same time, the e-AD is transferred to the Member State of destination and forwarded to the consignee. When the consignee receives the excise goods, he submits a receipt to the Member State of destination, who validates the data submitted and sends it back to the consignee. A copy of the receipt is transmitted to the Member State of dispatch that forwards it on to the consignor.

Essentially, the EMCS allows for a system of double bookkeeping. If the amount of excise goods and corresponding liability reported by the consignor does not match with the amount of excise goods received by the consignee, the transaction will be highlighted in the system. This reinforces the incentives for self-compliance as on the one hand, the consignor has the interest to acquit his liability but on the other hand, the consignee has no interest in acquiring a higher liability. In the case of import and export of excise goods, the EMCS is embedded in the NCTS (New Computerized Transit System), a computerized system for the declaration of customs.

The EMCS works in real time such that, the e-AD, necessary to dispatch goods, is submitted by the competent authority within a matter of hours. Consignors and consignees can participate in the EMCS either by an internet-based application (IEA) or by using software developed by a certificated third party. The former is provided free of charge by the European Union. The latter is a commercial product which entails both installation and ongoing operating costs.

2.3.2. Reporting of production, processing, and storage

The Directive (DIR 2008/118/EEC), leaves discretion to the Member States to lay down reporting standards for the stock of excise goods. In general, purchases and sales of excise goods have to be

³⁶ Rob Preece, Key Controls in the Administration of Excise Duties, *World Customs Journal*, Vol 2 No 1.

³⁷ Harald Jatzke, Production, holding and movement of excise goods under duty suspension within the European Union, *World Customs Journal*, Vol. 6 No 2, p. 5 et seq.

recorded by warehouse keepers via stock books.³⁸ However, it might be sufficient to use standard business records, as long as tax issues are not at risk.³⁹ These records are then audited periodically by the relevant authorities.

While requirements differ between Member States, periodic stocktaking is also required. For example, German excise law requires annual stocktaking⁴⁰ whereas Irish and UK excise law requires that licenced entities submit a monthly stock return for each warehouse.⁴¹ If any discrepancies can be detected, enforcement measures are enacted and payment of any excise owing made⁴².

Excise liabilities must also be monitored as they move through the manufacturing process. In this case the relevant authority must be able to reconcile raw material inputs to final production of excisable goods. Experience with excise highlights a number of important considerations, including: the nature of the raw material, the efficiency of the production process in terms of converting raw material to final product and whether there are any processes (such as sampling, testing etc.) which require primary or final products to be consumed during the production process⁴³. The primary goal is to develop a recording system where raw materials and other inputs can be measured against final production figures, allowing the good to be traced through the production process. In some cases, ratios of raw inputs to final products have been established. Deviations from the expected ratio would see the licensee called to account, as it highlights the potential for undeclared excise.

Once an excisable good is manufactured as a finished product, for a number of reasons, liabilities may be adjusted, transferred or written off. For example, liabilities are deducted when excisable goods are exported or transferred to another tax warehouse. Furthermore, liabilities may be written off in the case of destruction or irrevocable loss.⁴⁴ Destruction can occur due to the properties of the good, unforeseen events, force majeure or the authorisation by a competent authority. In these cases, excise duty does not have to be paid if the warehouse keeper can prove that the deficiencies

³⁸ Cf. Sec. 9 BierStV; Regulation 24 of the Alcohol Products Tax Regulations 2004; Irish Tax and Customs, Excise Revenue's Guide for Tax Warehousekeepers (Alcohol Products), Notice No 1877, Version July 2014, Section 10 and Appendix 1; Irish alcohol excise law requires the following records: Invoices, credit notes, debit notes, receipts and other records of payment, records relating to all alcohol products received and delivered, including those in relation to imports and exports, statements of account, profit and loss, trading and management accounts and reports, balance sheets and trading forecasts, production schedules and reports, and other records relating to such schedules and reports, production schedules and reports, and other records relating to such schedules and reports, stock accounts and other stocktaking records, including those relating to measurement of quantity and strength, records relating to any relief from, or repayment of, tax and to any claim for such relief or repayment, internal and external auditors reports, any other record relating to alcohol products, which is kept for a business purpose (Regulation 21 of the Alcohol Products Tax Regulations 2004 and Schedule 3).

³⁹ Cf. Sec. 9 (2) sentence 3 BierStV;

⁴⁰ Sec. 11 BierStV, Sec. 17 (1) BranntweinStV, Sec. 15 (4) EnergieStDV, Sec. 16 (1) SchaumwZwStV, Sec. 32 (1) TabStV.

⁴¹ Cf. Irish Tax and Customs, Excise – Revenues Guide for Tax Warehousekeepers (Alcohol Products), Notice No 1877, Version July 2014, p. 10.

⁴² Cf. Sec. 161 AO; Article 102 (2) Finance Act 2001 (Ireland); Irish Tax and Customs, Administration and Control of Tax Warehouses Manual – Part 1- General Warehousing Provisions, Section 3.6.5.

⁴³ Rob Preece, Key Controls in the Administration of Excise Duties, *World Customs Journal*, Vol 2 No 1.

⁴⁴ Matthias Bongartz, Trade in goods subject to excise duties which have been released for consumption in other Member States, *World Customs Journal*, Vol 6 No 2, pp. 19-28.

were due to fortuitous events or force majeure.⁴⁵ Alternatively, adjustments are also made for excisable goods which are consumed within a tax warehouse, for which liabilities must be paid.

2.3.3. Stakeholder input

Recording on production levels, sales and transportation of goods are an essential component of long established protocols. Therefore, industry participants did not consider the reporting requirements within the excise administration system to be much in addition to reporting that most companies already do as part of industry best practice. In addition, a number of stakeholders considered the reporting procedures to be a useful “stick” to ensure some businesses follow proper accounting standards. The implementation of accounting standards in some cases can assist businesses understand where inefficiencies lie and hence improve profits. Furthermore, industry participants also considered the EMCS to be a useful system for monitoring the transportation of excisable goods under duty suspension and acknowledged that it provided an effective balance between the revenue concerns of authorities and business concerns of companies.

Key learnings

Within excise it appears as though reporting requirements in many cases are only marginally additional to those activities already carried out under standard business reporting. Hence, in developing a consumption charge, reporting arrangements should align to or build from existing practices.

The EMCS represents a cost effective system which introduces a form of double book keeping. It is considered a good model for monitoring the movement of goods under duty suspension arrangements.

2.4. Compliance and enforcement

In regions such as Europe, excise charges are normally administered by relying on self-assessment. Government agencies seek to ensure compliance through verification actions such as audits, unannounced site visits and stock takes.

Key learnings

Efficient compliance requires a balance between the cost of monitoring and enforcement and the risks of non-compliance.

2.5. Other Issues - Exemptions and De Minimis Thresholds

The *de minimis* principle reflects a trade-off between losses in economic efficiency from preferential treatment of low value goods and gains in economic efficiency from reducing the administrative and compliance costs for governments and business. *De minimis* regimes have been applied in excise and

⁴⁵ Irish Tax and Revenue, Notice No 1877, Version July 2014, Section 16.3; Sec. 161 AO; Thilo Cöster in Armin Pahlke and Ulrich Koenig, *Abgabenordnung*, 2nd ed. 2009, Rn. 20.

customs to provide streamline border clearance and exemptions from duties and other taxes⁴⁶. Examples of these regimes are provided in the points that follow.

2.5.1. Minimum throughput required for warehouses used for storage purposes

To reduce administrative costs to government, national excise law requires a tax warehouse to reach a certain minimum throughput of excise goods within a fixed period of time. For example, United Kingdom excise law requires either a minimum potential duty liability of £500,000 on the average monthly stockholding of duty-suspended excise goods or a duty liability of at least £2,000,000 on an annual throughput of duty-suspended excise goods.⁴⁷ Under German excise law, no permit for a storing tax warehouse will be granted, if the annual throughput of beer/spirits/sparkling wine is less than 5.000 hl/50 hl/100 hl of beer/spirits/sparkling wine or the stockholding period is less than 1,5 months.⁴⁸

2.5.2. Exemptions from excise and de minimis rules

Directive 2008/118/EC provides exemptions if excise goods are intended to be used: in the context of diplomatic relations; by international organisations; by armed forces; for consumption under an international agreement (Article 12 para 1 DIR 2008/118/EC); or if excise goods are supplied by tax-free shops or on board of aircrafts (Article 12 para 1 and 2 DIR 2008/118/EC). In addition, specific Directives provide additional exemptions, mostly connected to a predetermined use of excise goods. For example, alcohol is exempt from excise if used for the production of medicines or for the manufacture of any product not for human consumption.

The Council Directive on the harmonization of structures of excise duties on alcoholic beverages sets *de minimis* rules, which exempt products for human consumption which contain only minimal levels of alcohol. Therefore, alcohol is exempt when used for the preparation of flavours, preparation of foodstuffs and beverages with an alcoholic strength not exceeding 1.2 % vol.⁴⁹

Under German excise law, exempted users of excise goods can either apply to gain the status of an authorised warehouse keeper or apply for the status of a registered user. In the latter case, reporting requirements for the movement and storage of excise products apply. Thus, alcohol can be moved under duty suspension arrangement from a tax warehouse, where alcohol is produced, to the premises of, for example, a chocolate manufacturer who holds a permit as registered user.⁵⁰ In this case, the consignor has to submit an application about the delivered goods with reference to delivery note numbers to the exempted user at the end of each month. The exempted user must then forward the document to the relevant authorities which verify the data submitted. If no objections

⁴⁶ Stephen Holloway and Jeffrey Rae, De minimis thresholds in APEC, *World Customs Journal*, Vol 6 No 1, pp. 31-62.

⁴⁷ HMRC, Notice 196 (October 2012), Excise goods: authorisation of warehouse keepers and approval of premises, 4.1.

⁴⁸ Sec. 5 (2) BierStV; Sec. 5 BrStV; Sec. 5 SchaumwZwStV

⁴⁹ Article 27 (1) lit. e) DIR 92/83/EEC.

⁵⁰ Sec. 139 (1) No 2 Gesetz über das Branntweinmonopol.

arise, the document will be submitted back to the exempted user who has to hand over a copy of the document to the consignor.⁵¹

In terms of reporting, the registered user has to record incoming and outgoing goods⁵² and the use of products.⁵³ Nevertheless, the relevant authorities can determine that commercial business records are sufficient for excise purposes.⁵⁴ Furthermore, annual stock taking is required.⁵⁵

2.5.3. Simplified procedures for duty-suspended movements

Article 30 DIR 2008/118/EC allows for simplified procedures for the movement of excise under duty suspension arrangement if the movement takes place entirely within a Member State. For example, simplified reporting is granted for movement that takes place between two warehouses of the same authorised warehouse keeper within a Member State. Furthermore, for movement within some Member States, licenced entities are exempt from EMCS reporting procedures. In addition, simplified procedures are possible for frequent movements between the territories of two or more Member States (Article 31 DIR 2008/118/EC). As an example, in some cases, simplified procedures are granted for the transport of energy products through pipelines.⁵⁶

2.5.4. De minimis thresholds for reporting

Similarly, most countries apply some form of customs reporting threshold, where goods that fall below a certain value threshold are subject to simplified reporting requirements⁵⁷. For example, goods imported into Australia with a value of less than AUD 1,000 do not attract charges and are subject to streamlined Self Assessed Clearance procedures. It has been estimated that such *de minimis* thresholds save businesses over 1 billion annually⁵⁸.

Key Learnings

De minimis thresholds are an effective means of avoiding high administrative costs associated with the control of small liabilities.

Applying de minimis thresholds may keep companies which only handle very small liabilities outside of the scheme.

De minimis can be applied to outright exemptions, reduced licencing requirements, and reduced reporting procedures.

⁵¹ Cf. Sec. 28 (4) BrStV.

⁵² Sec. 47 (2), 12 (3) BrStV.

⁵³ Sec. 47 (1) BrStV.

⁵⁴ Sec. 47 (2) sentence 2 BrStV.

⁵⁵ Sec. 48 (3) BrStV.

⁵⁶ Such simplified procedures have to be established by bilateral agreements between Member States and apply in the following countries: Austria, Czech Republic, Germany, France, Italy, Lithuania, Netherlands, Romania, Slovakia (Committee on excise duties, February 2014, Working Paper, TAXUD/308253/2009, Option 9 p. 16 et seq.).

⁵⁷ Stephen Holloway and Jeffrey Rae, *De minimis thresholds in APEC*, *World Customs Journal*, Vol 6 No 1, pp. 31-62.

⁵⁸ Centre for International Economics, *The GST Threshold for low value products*, Prepared for Conference of Asia Pacific Express Carriers (2011).

3. ADMINISTERING THE INCLUSION OF CONSUMPTION

3.1. General approach

3.1.1. Scope

Drawing on the experience with the excise system, the scope of the Inclusion of Consumption scheme must be clearly defined, in terms of the products and product classes which trigger liabilities, the industry participants which can process these products under duty suspension arrangement as well as the activities which can be carried out under duty suspension.

The scheme should focus on specific carbon intensive commodities like steel or clinker (for cement). These basic materials are produced by a limited number of relatively large production plants such that the scheme will cover a large proportion of CO₂ emissions⁵⁹ at relatively low administrative cost.

In each of these sectors it will be important to define the point in time when a carbon liability has been created. With reference to steel production, interviews with industry experts suggested at the point of hot rolling of steel would be an appropriate delineation. In the case of cement a liability would be created with the production of clinker.

Duty suspension arrangements should apply so the charge can be placed close to the point of final consumption. To facilitate duty suspension, those dealing in carbon intensive products must register as entities comparable with tax warehouses and warehouse keepers. Finally, duty suspension arrangement should only apply for the production, processing, holding and movement of goods. Accordingly, duty on any carbon intensive products that are consumed by a registered entity or used for production equipment or wasted in the production process must be paid by that registered entity.

3.1.2. Duty suspension arrangements: defining the Consumption Sphere

Drawing on the experience with the excise system, the administration of the Inclusion of Consumption into the EU ETS could work as follows. To allow European producers, manufactures or traders to handle carbon intensive products under duty suspension arrangements, they must register as Carbon Keepers and their premises as Carbon Warehouses. If carbon intensive products are stored, held or processed by registered companies, no charge is levied. Similarly, when carbon intensive products are traded between two Carbon Keepers, these products can be placed under suspension arrangement and no duty is charged. When these products are sold to unregistered entities or to the final consumer, the good is assumed to have entered the Consumption Sphere and the charge must be levied by the registered entity and passed onto the consumption price. The charge would be calculated according to the weight of the carbon intensive good (or the weight of the carbon intensive component e.g. of steel in a car), a BAT benchmark and the carbon price at the time when the product is released for consumption.

⁵⁹ Roland Ismer and Karsten Neuhoff, Border tax adjustment: a feasible way to support stringent emission trading, *Eur J Law Econ* (2007) 24, p. 153.

3.1.3. Imports and exports

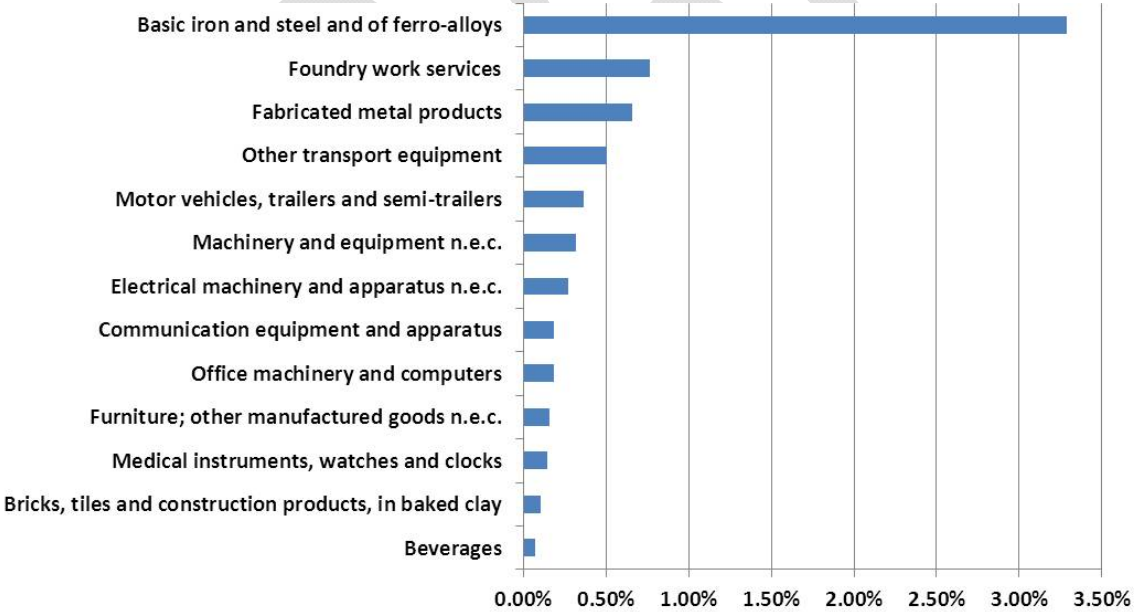
In the case of import, no charge will be levied if the carbon intensive product is received by a registered entity. In this case, the product has not yet been released for consumption. However, if a non-registered entity or a final consumer receives the product, the charge has to be levied by the customs authority. If a registered entity exports carbon intensive products, these products can be placed under duty suspension arrangement and can leave the territory of the European Union free of charge.

In calculating the charge, entities will be required to report on the weight of carbon intensive materials contained in exported and imported goods. This weight would then be converted to a liability (in the case of imports) or a deduction (in the case of exports) via pre-existing BAT benchmarks used for the free allocation of allowances and the carbon price.

3.1.4. De minimis exemptions

Consistent with other schemes, it would be reasonable to exclude some imports from the Inclusion of Consumption based on *de minimis* grounds. A threshold could be set based on the ratio of the value of the product’s carbon content (measured in EU ETS prices) and the (customs) value of the product itself. Products with a ratio below the threshold would be excluded from the scheme and could thus be imported into the European Union without triggering carbon liabilities. As an example, Figure 1 depicts the measure for traded commodities containing steel for a carbon price of €20/t CO₂.

Figure One: Carbon content (priced at €20/t CO₂) relative to product value of traded commodities



Note: Assumes a carbon price of €20
 Calculations based on data provided by Arjan Koning and Arnold Tukker

For simplification, only products from relevant product categories should be subject to individual reporting requirements. Thus for all product categories according to the Standard International Trade Classification (SITC) it would need to be estimated whether the threshold level is exceeded. Only for products in thus identified SITC codes would the importer have to report on the weight of steel

contained in the imported good (for primary and semi-finished products this is already reported). In contrast, the importer would not have to fulfil reporting requirements for products outside these categories.

Existing trade data published by Eurostat based on the categories of the ProdCom list can provide a starting point for the identification of the relevant SITC codes. It allows – based on Multiple Region Input Output Tables – to determine the content of steel (or of selected other carbon intensive commodities) per product value of traded good.

To account for changes in production processes and commodity prices, the list of relevant SITC codes would need to be updated periodically. Such a process could be aligned to the revision of the carbon leakage list, which takes place every five years.

Recommendation

- *The Inclusion of Consumption should focus on specific carbon intensive commodities like steel or clinker (for cement).*
- *Carbon liabilities are created with the production or importation of products from these sectors.*
- *The Charge would be calculated according to the weight of the carbon intensive good, pre-existing European best available technology benchmarks and the EU ETS permit price at the time when the product is released for consumption.*
- *Duty suspension arrangements which allow for producers, manufactures or traders to handle carbon intensive products charge free should be available to registered entities.*
- *De minimis thresholds should apply to imports listed with a small carbon value to product value ratio. Such thresholds can be implemented through the ProdCom list such that those product categories that do not meet the threshold are exempt from the scheme. The list should be revised in five year periods in parallel with the Carbon Leakage List.*

3.2. Administration

A framework for administration and control of the Inclusion of Consumption in the EU ETS has to cover the following administrative requirements:

- licencing and registration;
- monitoring, reporting and verification; and
- compliance and enforcement efforts.

These issues are briefly discussed in the sections that follow.

3.2.1. Licencing and registration as systemic requirement of duty suspension schemes

Duty suspension requires those entities dealing in the production, transportation and storage of goods to be licenced. In addition, licencing and registration provides an effective demarcation between Consumption and Production Spheres. Furthermore, licencing and registration provides national authorities with some control mechanism to ensure that carbon liabilities are accounted for correctly and no evasion of the charge takes place.

While the exact registration requirements would be agreed upon by the relevant authority and carbon intensive sector, drawing on experience with excise administration and control, requirements could encompass:

- the creation and maintenance of business records to a specific standard;
- access to business records, the licenced premise, or other relevant business apparatus;
- notification of changes to business activities or structure; and
- lodgement of appropriate security for the liability⁶⁰.

The stringency of licencing requirements is a key consideration for any administrative system. A rule of thumb applied in other sectors, is to impose stricter requirements on those entities which create or handle larger liabilities. Applied to the steel sector, this would imply that major steel producers would be subject to more stringent licencing arrangements than those downstream entities, which use steel in the production of final goods.

Importantly, licencing requirements should be integrated into existing reporting protocols, such that the additional reporting is kept to a minimal. Furthermore, as is common with the excise administration systems, the relevant authority could provide access to help desks, standardised forms, online tutorials and staff visits to assist in the application process.

Recommendation

Licenses for Carbon Keepers should be granted on the following conditions:

- *adoption of minimum accounting standards;*
- *records of stock and movement of duty suspended carbon intensive products;*
- *compliance with other fiscal obligations (direct taxation, customs, VAT);*
- *compliance with the requirements laid down by the Member State within whose territory an entity is situated;*
- *notification of changes to business activities or structure; and*
- *guarantees, if fiscal interests are at risk.*

Licenses for Carbon Warehouses be granted on the following conditions:

- *details of the address and a description of the premises that is to be licensed as a Carbon Warehouse are provided;*
- *details of the stock reporting system are provided; and*
- *records, for each Carbon Warehouse of stock and movement of carbon intensive products are kept.*

3.2.2. Monitoring, reporting and verification

Recording and reporting are necessary to ensure that the carbon liabilities which have been created have been correctly acquitted. Key to the reporting arrangements is that the amount of liability paid and held under suspension arrangement reflects the level of liability created in the overall system. This can be verified by a periodic reporting schedule, where deliveries, sales, and stocks of carbon

⁶⁰ Rob Preece, Key Controls in the Administration of Excise Duties, *World Customs Journal*, Vol 2 No 1.

intensive products over the specified period are reported. Alignment to existing business reporting will also reduce the additional reporting required.

Movement of steel and intermediary products

Conceivably, a CMCS, similar in design to the EMCS (discussed above) could be developed.⁶¹ In establishing the CMCS, it would first be necessary to establish a European wide database similar to SEED, which contains all licenced entities in the scheme. A unique identification number would be assigned to each licenced entity. The creation and movement of goods by or between entities is then tracked and liabilities deducted or added to the license's accounts. Being electronic, transactions can be monitored by the relevant authority with discrepancies highlighted and investigated.

As applied in excise, simplified procedures could be implemented for transactions which are only conducted within one Member State or for regular and frequent movement of goods between two or more Member States.

Production, processing and storage

Carbon liabilities which are created through production and the importation of carbon intensive goods can be reported under the CMCS through reference to standard business records or transactions conducted with the relevant customs authority. These records are largely already kept for tax or business purposes and published in quarterly and annual reports⁶² such that the additional reporting requirement under the CMCS would be marginal⁶³.

Downstream manufactures and producers will also be required to enter the weight of duty suspended carbon intensive goods into the CMCS. Specifically, the weight of incoming, outgoing and stored duty suspended products would be recorded and reported such that at the end of the reporting period a liability for each registered entity can be drawn from the CMCS. While it is common in the excise sector to report separately on an excise product that is destroyed or written off, it is not clear that this would be necessary under the Inclusion of Consumption approach – any carbon intensive products that were wasted in the production process would trigger a liability for the registered entity.

Interviews with the steel sector suggested that for most firms, reporting requirements would be met relatively easily within existing business practices. That said, there was some concern that for smaller firms without existing electronic reporting structures, there may be some additional costs. Furthermore, several stakeholders noted that reporting on steel production and sales, differentiated by product type may generate commercial confidentiality concerns. However, such granular reporting would not be required. Rather, only reporting on the generic weight of carbon intensive

⁶¹ While such a system was developed in excise to control flows of goods between registered companies, the concept could be applied to allow for reporting and monitoring of carbon liabilities from the point of creation to acquittal of carbon liability.

⁶² See for example Tata Steel 106th Annual Report 2012-2013, p112 or Volkswagen Group Annual Report, 2013, Key Figures.

⁶³ As the charge is calculated on the quantity of steel, accounting should focus on amount of steel contained within intermediary and final products, rather than the amount of steel products sold.

products would be necessary. At this aggregation level no commercial confidentiality concerns were reported in interviews.

Imported goods

At the time of import, the SITC category of a good is declared according to customs procedure. For pre-defined SITC categories (for which CO₂ consumption charge on steel exceeds threshold level of product value), an additional declaration of the weight of the steel contained in the import would be required. For several SITC categories – in particular semi-finished products – this is already declared by importers; for compound products which contain both materials covered by the scheme and others that are not covered, an additional reporting requirement on the weight of the materials covered by the scheme would have to be introduced. Based on this declaration the liability for the consumption charge would be allocated to the importer. Following standard customs procedure, the validity of declared information would be verified with spot checks.

Acquittal of carbon liability

Carbon liabilities are predominantly acquitted when carbon intensive products are sold to unregistered companies or final consumers. At this point, similar to excise, the charge has to be paid to the national trust fund at the end of each accounting period and the liability is removed from the accounts. Alternatively, carbon liabilities can be acquitted when carbon intensive products are exported outside of the European Union. In this case, once verified, the quantity of exported material is removed from the entities account and no duty is paid. In addition, liabilities associated with material that is lost, wasted or written off in the production process must also be acquitted. Such liabilities are to be paid by registered entities at the end of the reporting period and can be calculated directly from the CMCS.

Recommendation

- *A CMCS system should be established to track the movement of duty suspended carbon intensive goods.*
- *All warehouse keepers must report (in weight) production volumes, in going and outgoing movements and the level of storage of carbon intensive goods into the CMCS*
- *There shall be no write-offs for products lost or damaged during the production process.*
- *At the end of the reporting period, all warehouse keepers must pay duty on any duty suspended products that have been consumed within the production process.*
- *Simplified reporting procedures could be considered for trade within a Member state, regular bilateral trade between Member States, and movement between warehouses registered to the same Carbon Keeper.*

3.2.3. Other issues

Treatment of scrap

Scrap can either be melted down and recast into new products,⁶⁴ or in some instances refurbished and used again for example as construction material. Under the proposed approach, scrap metals will be excluded from the scheme such that no liabilities are attached to their importation or exportation. However, when scrap is melted and used for the production of hot rolled steel, the product is considered to be destroyed and a new liability created through the production process.

It is recognised that such treatment could provide opportunities for fraud. For example, carbon intensive products mislabelled as scrap metal could enter the European Union without bearing the charge. Alternatively, mislabelled scrap could be exported as final products to incorrectly acquit carbon liabilities.

One approach to avoid such behaviour is to require that scrap importers and exports register as “registered users” and keep books regarding the usage and further treatment of imported scrap. Since scrap is mainly imported by steel companies, which are already registered as carbon keepers, additional monitoring efforts and administrative costs would be minimal. Alternatively, monitoring efforts could be focuses on European external borders to verify that steel is not been declared as scrap to circumvent the liability for the consumption charge on steel.

Compliance and enforcement

For a number of reasons, relatively high rates of compliance could be expected with the Inclusion of Consumption, when compared to other consumption charges. Firstly, unlike excise goods, the consumption charge would only make up a minor proportion of the final value of the steel product. Secondly, as the charge would largely be determined by the carbon price it would be consistent across Member States. Hence, there would not be the incentive for illegal movement of goods between Member States to exploit difference across excise rates.

That said, any policy is only effective if it is correctly administered and enforced. The relevant authority would need to determine the necessary enforcement strategy. However, as a general approach, anti-abuse rules could be established. Anti-abuse rules are a broad and general set of principle-based rules aimed at reducing tax avoidance. Similar broad principles could be established to govern the Inclusion of Consumption, to reduce the incentive to invent schemes aimed at circumnavigating or benefiting from the charge. In addition, fines are to be imposed on any misuse of the scheme.

⁶⁴ Dieter Janke, Luben Savov, Hans-Jörn. Weddige, Eike Schulz, Scrap-based steel production and recycling of steel, *Mater. Technol* 34(6)387(2000), p. 389.

4. NEXT STEPS

This report explores a blue print for the administration and control of the “Inclusion of Consumption”. The proposed approach builds from the administration of other consumption based levies including excise and VAT. The intent is not to design an all-encompassing administrative framework, but rather to stimulate debate on how such a system may function. We very much look forward to receiving your comments.

DRAFT

Characteristics	Excise	Inclusion of consumption
Legal nature	Excise duties are taxes and are directly assigned to the national budgets.	The charge levied is a non-fiscal charge, which is linked to the EU ETS and constitutes a market-based approach. It is assigned to national trusts and strictly separated from the national budget.
Rate	Excise rates are fixed rates and differ within the Member States of the European Union.	The rate is linked to the carbon price at the time of release for consumption and the benchmark for carbon intensity of primary production of carbon intensive commodity
Point of time when goods are subject to the duty	Excise goods are subject to excise at the time of their production, extraction and importation	Carbon intensive goods are subject to the consumption-based charge at the time of their production or importation
Point of time of chargeability	Excise duties become chargeable at the time of release for consumption. Release for consumption refers to the departure of excise goods from duty suspension arrangements or the importation of excise goods.	The charge becomes chargeable at the time of release for consumption. Release for consumption refers to the departure of excise goods from duty suspension arrangements or the importation of carbon intensive goods, intermediaries or final goods.
Duty suspension arrangements	Duty suspension arrangements apply on the production, processing, holding or movement of excise goods.	Duty suspension arrangements apply on the production, processing, holding or movement of carbon intensive goods or intermediaries.
Tax warehouses and warehouse keepers	Tax warehouses are spatially defined areas in which excise goods can be produced, processed, received or dispatched under duty suspension arrangements. Some Member States do not issue tax warehouse licenses if a monthly or annual minimum throughput is not met.	Carbon Warehouses are spatially defined areas in which carbon intensive goods and intermediaries can be produced, processed, received or dispatched under duty suspension arrangements.
De minimis thresholds	De minimis rules apply to certain products, irrespective of being domestically produced or imported to the European Union	A de minimis thresholds apply to imported products which only contain a certain amount of carbon intensive goods. Such a threshold can be based on the ratio of value of the carbon stored within a product and the value of the product itself.
Monitoring	The EMCS is used to track and trace trade flows of excise goods under duty suspension arrangement.	The CMCS is used to track and trace trade flows of carbon intensive and intermediary products. In addition, the CMCS can be used for accounting purposes.

Glossary of Terms

Authorized Warehouse Keeper	Natural or legal person authorized by the competent authorities of a Member State, in the course of his business, to produce, process, hold, receive or dispatch excise goods under duty suspension arrangements in a tax warehouse.
BAT	Best Available Technology
Carbon Keeper	Natural or legal person authorized by the competent authorities of a Member State, in the course of his business, to produce, process, hold, receive or dispatch carbon intensive goods under duty suspension arrangements in a Carbon Warehouse.
Carbon Warehouses	Place where carbon intensive goods are produced, processed, held, received or dispatched under duty suspension arrangements by a carbon keeper in the course of his business, subject to certain conditions laid down by the competent authorities of the Member State where the Carbon Warehouse is located.
CMCS	(Carbon Movement and Control System) Electronic track and trace system to monitor and account for trade flows of carbon intensive goods and intermediary products.
e-AD	Electronic Administrative Document
EMCS	(Electronic Movement and Control System) Electronic track and trace system to monitor excise flows under the European excise scheme.
NCTS	New Computerized Transit System
ProdCom List	Production Communautaire List ; classification of industrial products which includes more than 4,500 headings.
Registered Consignee	Natural or legal person authorised by the competent authorities of the Member State of destination, in the course of his business and under the conditions fixed by those authorities, to receive excise goods moving under a duty suspension arrangement from another Member State.
Registered Consignor	Natural or legal person authorised by the competent authorities of the Member State of importation, in the course of his business and under the conditions fixed by those authorities, to only dispatch excise goods under a duty suspension arrangement upon their release for free circulation in accordance with Article 79 of Regulation (EEC) No 2913/92;
Release for free Circulation	Customs procedure which confers on non-Community goods the customs status of Community goods.
System of Exchange of Excise Data	Database containing excise registration number of authorized warehouse keepers, registered consignees and registered consignors.
Tax Warehouse	Location where excise goods are produced, processed, held, received or dispatched under duty suspension arrangements by an authorised warehouse Keeper in the course of his business, subject to certain conditions laid down by the competent authorities of the Member State where the tax warehouse is located.
VAT	Value Added Tax

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