

Inclusion of Consumption into the EU ETS: The Legal Basis under European Union Law

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Traditionally discussed measures to prevent carbon leakage under the European Union (EU) emissions trading system, such as the free allocation of allowances or border carbon adjustments, either suffer from significant economic drawbacks or have seen their political, legal and administrative feasibility questioned. Recently, a novel approach has been proposed in the form of the inclusion of consumption into emissions trading schemes. Under this approach, a charge would be imposed on carbon-intensive products at the time of their release for consumption within the EU. After sketching this proposal, this article discusses the correct legal basis under EU law. It develops the argument that the inclusion of consumption may be based on Article 192.1 of the Treaty on the Functioning of the EU and thus be adopted without unanimity voting in the Council of the EU.

INTRODUCTION

Under the European Union emissions trading system (EU ETS),¹ operators of covered installations have to acquire and retire emission permits for each tonne of greenhouse gases emitted during the production process.² The key idea of the scheme is to reduce emissions in a cost-effective and economically efficient way.³ This requires the cumulative operation of two channels, namely: (i) upstream production efficiency in the sense that least-cost emissions reductions are pursued in the production process;⁴ and (ii) a price signal along the value chain, which sets incentives for the substitution

for lower-carbon products and for promoting innovation, while allocating mitigation costs to consumers.⁵

However, there is no single carbon price, but a plethora of prices, as the EU ETS is geographically limited to the territory of the EU⁶ and similar schemes, with varying degrees of stringency, exist only in some other regions.⁷ This spatial differentiation means that trade-exposed, energy-intensive industries may be induced to replace domestic production by imports, or to relocate production to foreign countries (also known as carbon leakage).⁸

Among the measures proposed to address carbon leakage,⁹ attention has largely focused on approaches which can be integrated in the emissions trading mechanism.¹⁰ They can be broadly classified into two different groups – free allocation of allowances and border carbon adjustments. Under free allocation,¹¹ emitters from sectors exposed to leakage receive a share or all of their required allowances for free (or, more generally, for a consideration below market price). Imported products remain outside the scope of the emissions trading scheme. Free allocation, which can be based on historic data or actual output,¹² seeks to improve the competitive position of domestic products through a reduction of the financial costs borne by

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¹ Directive 2003/87/EC of 13 October 2003 Establishing a Scheme for Greenhouse Gas Emission Allowance Trading within the Community and Amending Council Directive 96/61/EC, [2003] OJ L275/32, as amended by Directive 2009/29/EC of 23 April 2009 Amending Directive 2003/87/EC so as to Improve and Extend the Greenhouse Gas Emission Allowance Trading Scheme of the Community, [2009] OJ L140/63.

² *Ibid.*, Article 12.3.

³ *Ibid.*, Article 1; see also ECJ, Joined Cases C-566/11, C-567/11, C-580/11, C-620/11 and C-640/11, *Iberdrola, SA and Others v. Administración del Estado*, ECLI:EU:C:2013:660, at paragraph 43 (*Iberdrola, SA*).

⁴ See M. Grubb, J. Hourcade and K. Neuhoff, *Planetary Economics* (Routledge, 2014), at Chapter 6 on pricing pollution and at Chapter 7 on cap-and-trade and offsets.

⁵ *Iberdrola, SA*, n. 3 above, Opinion of Advocate General (AG) Kokott delivered on 21 March 2013 ('Opinion of AG Kokott, *Iberdrola, SA*'), at paragraph 70; Commission of the European Communities, Green Paper on Greenhouse Gas Emissions Trading within the European Union, COM(2000) 87, at paragraph 7.3; R. Ismer, *Klimaschutz als Rechtsproblem* (Mohr Siebeck, 2014), at 104.

⁶ As well as Iceland, Liechtenstein and Norway.

⁷ For an overview, see C. Serre *et al.*, *Emissions Trading Worldwide: ICAP Status Report 2015* (ICAP, 2015), at 20ff.

⁸ See S. Dröge *et al.*, *Tackling Leakage in a World of Unequal Carbon Prices* (Climate Strategies, 2009); F. Sindico, 'The EU and Carbon Leakage: How to Reconcile Border Adjustments with the WTO?', 17:6 *European Energy and Environmental Law Review* (2008), 328.

⁹ For an overview on carbon leakage and potential countermeasures, see S. Dröge *et al.*, n. 8 above.

¹⁰ On subsidies as an allocation instrument, which, however, does not alter the marginal incentives for shifting production to regions with lower carbon costs, see, e.g., *ibid.*, at 54.

¹¹ See, e.g., P. Quirion, 'Historic Versus Output-based Allocation of GHG Tradable Allowances: A Comparison', 9:6 *Climate Policy* (2007), 575; S. Dröge *et al.*, n. 8 above, at 46–54.

¹² A comparison of both is given by P. Quirion, n. 11 above.

domestic installations (downward levelling).¹³ In contrast, border carbon adjustments¹⁴ extend the financial burden borne by domestically produced goods to imported goods. Border adjustments thus seek to eliminate the competitive disadvantage of domestic production through an increase of the financial costs borne by foreign produced goods (upward levelling).¹⁵ In order to fend off the accusation of protectionism, the upward levelling must not exceed the hypothetical costs the product would have borne had it been produced domestically.¹⁶

Both the free allocation of allowances and border carbon adjustments have been criticized in the scholarly literature. Free allocation of allowances based on actual output (output-based allocation) would dampen the price signal and hence remove incentives for emission reductions along the value chain.¹⁷ By contrast, free allocation based on a historic reference base, which was the initial approach under the EU ETS, led to economic inefficiencies like over-allocation¹⁸ and windfall profits,¹⁹ and encouraged economic agents to engage in strategic gaming behaviour.²⁰ Border carbon adjustments, although economically sound,²¹ might in turn face legal and political constraints.²²

¹³ See S. Dröge *et al.*, n. 8 above, at 46ff.

¹⁴ See, e.g., H. van Asselt and F. Biermann, 'European Emissions Trading and the International Competitiveness of Energy-intensive Industries: A Legal and Political Evaluation of Possible Supporting Measures', 35:1 *Energy Policy* (2007), 497, at 502; R. Ismer and K. Neuhoff, 'Border Tax Adjustments: A Feasible Way to Support Stringent Emission Trading', 24:2 *European Journal of Law and Economics* (2007), 137.

¹⁵ See S. Dröge *et al.*, n. 8 above, at 55ff.

¹⁶ See, e.g., R. Ismer and K. Neuhoff, n. 14 above, at 148ff.

¹⁷ M. Grubb and K. Neuhoff, 'Allocation and Competitiveness in the EU Emissions Trading Scheme: Policy Overview', 6:1 *Climate Policy* (2006), 7, at 25; R. Ismer, n. 5 above, at 180.

¹⁸ L. Clarke *et al.*, 'International Climate Policy Architectures: Overview of the EMF 22 International Scenarios', 31:2 *Energy Economics* (2009), 264; K. Neuhoff and A. Schopp, 'Europäischer Emissionshandel: Durch Backloading Zeit für Strukturreform gewinnen' (DIW, 2013), at 4ff.; B. Borkent *et al.*, *Dynamic Allocation for the EU Emissions Trading System: Enabling Sustainable Growth* (Ecofys, 2014), at 1; R. Ismer, n. 5 above, at 172.

¹⁹ C. Hepburn *et al.*, 'Auctioning of EU ETS Phase II Allowances. How and Why?', 6:2 *Climate Policy* (2006), 137, at 140; P. Quirion, n. 11 above, at 581ff.; R. Ismer, n. 5 above, at 179.

²⁰ F. Branger *et al.*, *EU ETS, Free Allocations and Activity Level Thresholds: The Devil Lies in the Details* (Centre for Climate Change Economics and Policy and Grantham Research Institute on Climate Change and the Environment, 2014).

²¹ See the meta-analysis of 25 articles related to carbon leakage estimations by F. Branger and P. Quirion, 'Would Border Carbon Adjustments Prevent Carbon Leakage and Heavy Industry Competitiveness Losses? Insights from a Meta-analysis of Recent Economic Studies', 99 *Ecological Economics* (2014), 29.

²² For a recent overview, see K. Holzer, *Carbon-related Border Adjustment and WTO Law* (Edward Elgar, 2014). For arguments in favour of the legal adjustability of carbon costs, see F. Biermann and R. Brohm, 'Border Adjustments on Energy Taxes: A Possible Tool for European Policymakers in Implementing the Kyoto Protocol', 74:2 *Vierteljahreshefte zur Wirtschaftsforschung* (2005), 249, at 251ff.; R. Ismer and K. Neuhoff, n. 14 above, at 137–164; R. Ismer, n. 5 above,

These deficiencies of free allocation and border carbon adjustments make it necessary to search for new and viable solutions to combating carbon leakage which comply with current climate policy objectives as well as European and international law. Such a solution could arguably take the form of including consumption into the EU ETS.²³ In essence, this would mean that the release for consumption of goods covered would be subject to a charge reflecting the EU ETS allowance price. A key challenge for the inclusion of consumption would be its legal and political feasibility, in particular with respect to its adoption in the Council of the EU. The failure of the Commission's carbon tax proposal in the 1990s,²⁴ which would have required unanimity in the Council, clearly illustrates that some countries²⁵

at 419. For arguments against the legal feasibility of carbon costs, see R. Quick, 'Border Tax Adjustment' in the Context of Emission Trading: Climate Protection or "Naked" Protectionism?', 3:5 *Global Trade and Customs Journal* (2008), 163, at 164–166. See also J. de Cendra, 'Can Emissions Trading Schemes be Coupled with Border Tax Adjustments? An Analysis vis-à-vis WTO Law', 15:2 *Review of European Community and International Environmental Law* (2006), 131, at 139ff.; F. Sindico, n. 8 above, at 337. On the 'like product' discussion in the context of the World Trade Organization (WTO), see, e.g., F. Biermann and R. Brohm, 'Implementing the Kyoto Protocol without the USA: The Strategic Role of Energy Tax Adjustments at the Border', 4:3 *Climate Policy* (2005), 289, at 291ff.; R. Quick and C. Lau, 'Environmentally Motivated Tax Distinctions and WTO Law: The European Commission's Green Paper on Integrated Product Policy in the Light of the "Like Product" and "PPM" Debate', 6:2 *Journal of International Economic Law* (2003), 419, at 424–436; C. Kaufmann and R. Weber, 'Carbon-related Border Tax Adjustment: Mitigating Climate Change or Restricting International Trade', 10:4 *World Trade Review* (2011), 497, at 506–510. On the calculation of border carbon adjustments, see, e.g., R. Ismer, n. 5 above, at 420ff.; J. de Cendra, n. 22 above, at 142. On the justification of border carbon adjustments, see, e.g., R. Ismer and K. Neuhoff, n. 14 above, at 149–152; R. Quick, n. 22 above, at 168–174; C. Kaufmann and R. Weber, n. 22 above, at 511–520. On the administrative challenges, see, e.g., R. Ireland, 'Implications for Customs of Climate Change Mitigation and Adaptation Policy Options: A Preliminary Examination', 4:2 *World Customs Journal* (2010), 21, at 27ff.; S. Monjon and P. Quirion, 'How to Design a Border Adjustment for the European Union Emissions Trading System?', 38:9 *Energy Policy* (2010), 5199, at 5203ff.; M. Moore, 'Implementing Carbon Tariffs: A Fool's Errand?', 34:10 *The World Economy* (2011), 1679; D. Helm, *The Carbon Crunch: How We're Getting Climate Change Wrong – And How to Fix It* (Yale University Press, 2012), at 191. On the political feasibility, see, e.g., T. Houser *et al.*, *Leveling the Carbon Playing Field: International Competition and US Climate Policy Design* (Peterson Institute for International Economics and World Resources Institute, 2008), at 42; S. Dröge *et al.*, n. 8 above, at 55 and 64.

²³ W. Acworth *et al.*, *Including Consumption in the EU ETS: Administrative Implementation of a Consumption Based Charge* (Climate Strategies, 2014).

²⁴ Commission of the European Communities, Proposal for a Council Directive Introducing a Tax on Carbon Dioxide Emissions and Energy, COM(92) 226. See also European Commission, Proposal for Council Directive Amending Directive 2003/96/EC Restructuring the Community Framework for the Taxation of Energy Products and Electricity, COM(2011) 169, which has not yet been adopted.

²⁵ See M. Lee, *EU Environmental Law: Challenges, Change and Decision-making* (Hart, 2005), at 191ff.; C. Streck and D. Freestone, 'The EU and Climate Change', in: R. Macrory (ed.), *Reflections on 30 Years of EU Environmental Law: A High Level of Protection?* (Europa Law, 2005), 87, at 98.

hold strong reservations with respect to any type of taxation at the European level. Thus, the inclusion of consumption would probably only be feasible if it can be passed without unanimity in the Council.

The present article argues that the inclusion of consumption may indeed be introduced without unanimity voting in the Council. For that purpose, the article first provides details on the proposed inclusion of consumption to the extent they are necessary for the following legal analysis. It then moves to the key part of this article, the in-depth discussion of the correct legal basis. In doing so, it demonstrates that Article 192 of the Treaty on the Functioning of the European Union (TFEU)²⁶ in conjunction with Article 191 TFEU would constitute the right legal basis. More specifically, Article 192.1 TFEU establishes an ordinary legislative procedure for environmental policy measures, whereas Article 192.2 TFEU requires unanimity in the Council for 'provisions primarily of a fiscal nature'. The article contends that Article 192.1 TFEU is the proper basis because the measure is not to be seen as based on 'provisions primarily of a fiscal nature' for two reasons: first, since the inclusion of consumption would form an integral part of the EU ETS, it would, just as the EU ETS generally, not be based on 'provisions primarily of a fiscal nature'. And, second, even if the inclusion of consumption could not be considered an integral part of the EU ETS, Article 192.2(a) TFEU would not apply, as the pertinent provisions still would not be, or at least not primarily be, of a fiscal nature.

INCLUSION OF CONSUMPTION IN THE EU ETS: MAIN FEATURES OF THE CONCEPT

The inclusion of consumption would subject the release for consumption of goods covered to a charge reflecting the carbon costs of the production of the good evaluated at the EU ETS allowance price. Leakage protection would then consist of two pillars. Under the first pillar, installations in trade-exposed sectors at risk of leakage²⁷ would continue to receive free allowances. To avoid distortional effects, the allocation rules would be changed to output-based allocation. The complementing second pillar, which represents the key element of the inclusion

of consumption, would add a consumption-based charge to the EU ETS Directive.

The scope of goods covered would be determined by the trade-off between the effectiveness of climate policy, which points to a large scope on the one hand, and compliance and administrative costs on the other. Thus, only sectors where the share of carbon costs relative to total value added surpasses a certain threshold level would qualify.²⁸ In practice, the charge would have to be imposed on specific sectors, such as conceivably aluminium, steel, copper, cement and potentially petrochemical refining.²⁹ This selection of goods would also reflect the aims of trying not to distort markets and to avoid any inter-substitution of carbon-intensive goods.

The level of the charge would reflect the carbon content of the good priced at the EU ETS carbon price. It would be calculated as the weight of the carbon-intensive good in tonnes, multiplied by a product-specific benchmark and by the average carbon price. The carbon intensity of goods would be determined by the same product-specific benchmarks that are used to determine free allocation. The carbon price would correspond to the market price of allowances. However, for reasons of cost-efficiency and administrative feasibility, a monthly or quarterly average of allowance prices would generally have to be applied. An earlier adjustment in case of significant changes in the allowance price could be required, e.g., if the carbon price rose or dropped by more than a specified percentage range.

The chargeable event would be defined as the production of covered goods. However, in line with standard excise practice,³⁰ the creation of a liability to the charge under the inclusion of consumption would have to be distinguished from the time when such a liability becomes due: the charge would not be due immediately upon production, but rather at the time of release for consumption within the EU.³¹ This means that under

²⁶ Consolidated Version of the Treaty on the Functioning of the European Union, [2012] OJ C326/47 ('TFEU').

²⁷ According to Article 10a of Directive 2003/87/EC as amended by Directive 2009/29/EC, n. 1 above, 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%.

²⁸ See, e.g., the seminal graph in M. Grubb *et al.*, n. 4 above, at 290.

²⁹ For detailed studies of the characteristics of the sectors, see M. Bergmann *et al.*, *Imposing a Unilateral Carbon Constraint on Energy-intensive Industries and its Impact on their International Competitiveness: Data and Analysis* (European Economy, 2007); K. Neuhoff *et al.*, *Carbon Control and Competitiveness Post 2020: The Cement Report* (Climate Strategies, 2014) ('Cement Report'); K. Neuhoff *et al.*, *Carbon Control and Competitiveness Post 2020: The Steel Report* (Climate Strategies, 2014).

³⁰ Directive 2008/118/EC of 16 December 2008 Concerning the General Arrangements for Excise Duty and Repealing Directive 92/12/EEC, [2009] OJ L9/12; see also H. Jatzke, 'Production, Holding and Movement of Excise Goods under Duty Suspension within the European Union', 6:2 *World Customs Journal* (2012), 3.

³¹ Directive 2008/118/EC, n. 30 above, Article 7.2 defines the release for consumption as 'any of the following:

(a) the departure of excise goods, including irregular departure, from a duty suspension arrangement;

so-called duty suspension arrangements, the products could be processed at several production levels and incorporated into other goods without the liability becoming due.³²

The treatment of imports and exports would correspond to the destination principle.³³ Liability would thus also be created upon importation of high carbon goods, intermediary goods and finished goods into the EU. For purposes of administrative feasibility, it would be reasonable to exclude imports from the scheme based on *de minimis* grounds.³⁴ While there would be no refund or return of allowances upon exportation, exports would be acquitted from the liability upon exportation. Exported goods continuously held under duty suspension arrangements since production would thus not be burdened under the scheme. This would reflect the fact that these goods would not be consumed within the EU, so that under the destination principle no charge should be levied there.

The money raised would be allocated to special funds, e.g., in the country in which the goods were released for consumption. To provide greater certainty that the charge does not fall under Article 192.2 TFEU, the funds would have to be separate from the general budget. They could be placed under the roof of an established organization.³⁵ Alternatively, new entities could be set up. The funds would use the revenue in the first place for purchasing allowances on the carbon markets to cover net imports. In such a way, all emissions linked to carbon-intensive products consumed within the EU

would be covered by allowances. The remainder of the funds would support climate mitigation or adaptation measures. The decisions on the exact usage of the funds, which would then have to be in line with EU State aid rules, as well as on the exact governance structures, could be taken at the national level.

From an economic perspective, the inclusion of consumption combined with output-based allocation would be largely similar to border carbon adjustments on imports – and, to the extent that a duty suspension arrangement applies, also on exports – with full auctioning of allowances.³⁶ Output-based allocation would ensure the carbon efficiency of upstream production and establish a level playing field between domestic and foreign producers. The charge under the inclusion of consumption would send a price signal along the value chain and thus create the incentive for downstream producers to invest in low-carbon technology. Furthermore, the equal treatment of imported and domestically produced products would contain the risk of carbon leakage. The charge would not differentiate according to the actual carbon intensity of foreign products, as there would be no such distinction for domestic products either. The equal treatment of domestic and foreign products would make the scheme almost automatically compliant with the law of the World Trade Organization (WTO).³⁷ All this means that the scheme would secure the economic benefits whilst addressing the concerns regarding administrative, legal and political feasibility as well as conformity with world trade law.

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- (b) the holding of excise goods outside a duty suspension arrangement where excise duty has not been levied pursuant to the applicable provisions of Community law and national legislation;
 - (c) the production of excise goods, including irregular production, outside a duty suspension arrangement;
 - (d) the importation of excise goods, including irregular importation, unless the excise goods are placed, immediately upon importation, under a duty suspension arrangement.

³² Under duty suspension arrangements, goods, prior to their release for consumption, can be moved within the EU under suspension of duty from a tax warehouse to various destinations, in particular to another tax warehouse. This means that the created liability does not become due as long as the goods are held under such arrangements. They are standard practice for excise; see *ibid.*, Articles 4, 7.1–2 and 17. For further details, see W. Acworth *et al.*, n. 23 above, at 18.

³³ The destination principle 'enable[s] exported products to be relieved of some or all of the tax charged in the exporting country in respect of similar domestic products sold to consumers on the home market and . . . enable[s] imported products sold to consumers to be charged with some or all of the tax charged in the importing country in respect of similar domestic products'. Report by the Working Party on Border Tax Adjustments (20 November 1970, L/3464), at paragraph 4.

³⁴ For further details, see W. Acworth *et al.*, n. 23 above, at 19ff.

³⁵ As an example for such a governance structure one may refer to the Global Environmental Facility (GEF), which is run under the auspices of the World Bank. See, e.g., GEF Secretariat, 'Instrument for the Establishment of the Restructured Global Environment Facility' (GEF, 2015).

ARTICLE 192.1 TFEU AS LEGAL BASIS FOR THE INCLUSION OF CONSUMPTION

The principle of conferral anchored in Articles 4.1 and 5.1 TEU³⁸ means that the EU may introduce the inclusion of consumption only if and to the extent that it has a legal basis for it. Article 192 TFEU allows comprehensive Union measures in the field of environmental policy with regard to the objectives listed in Article 191 TFEU.³⁹ The provision lays down a two-pronged legislative procedure: Article 192.1 TFEU only requires use

³⁶ See 'Cement Report', n. 29 above, at 42.

³⁷ Provided there is no covert discrimination. For the parallel discussion on border carbon adjustments, see n. 22 above.

³⁸ Consolidated Version of the Treaty on European Union, [2012] OJ C326/13 ('TEU').

³⁹ According to TFEU, n. 26 above, Article 191.1, 'Union policy in environmental matters shall contribute to pursuit the following objectives: preserving, protecting and improving the quality of the environment, protecting human health, prudent and rational utilisation of natural resources, promoting measures at international level to deal with regional or worldwide environmental problems, and in particular combating climate change.'

of the ordinary legislative procedure⁴⁰ (involving a qualified majority vote in the Council⁴¹). By contrast, for 'provisions primarily of a fiscal nature', Article 192.2(a) demands a unanimous vote in the Council.

In the following, we will demonstrate that the inclusion of consumption would not need to be based on 'provisions primarily of a fiscal nature'. A qualified majority in the Council would hence be sufficient. Two main arguments can be advanced. First, rather than constituting a separate measure, the inclusion of consumption has to be understood as an integral part of the EU ETS, the introduction of which did not require unanimity. Second, even if the inclusion of consumption could not be considered an integral part of the EU ETS, it would arguably still not be based upon 'provisions primarily of a fiscal nature', as this term has to be construed in a way to only comprise charges which are comparable with taxes in the narrow sense.

INCLUSION OF CONSUMPTION AS AN INTEGRAL PART OF THE EU ETS

The first argument for basing the inclusion of consumption on Article 192.1 TFEU so that it can be adopted with qualified majority vote instead of unanimity in the Council comes in two steps. First, the EU ETS itself was correctly based on Article 192.1 TFEU. Second, the inclusion of consumption would constitute an integral part of the EU ETS that addresses the problems of the system caused by free allocation as an anti-leakage measure. As the nature and the objective of the inclusion of consumption would be identical to those of the EU ETS as a whole, the inclusion of consumption could thus also be based on Article 192.1 TFEU.

EU ETS not Based on 'Provisions Primarily of a Fiscal Nature'

The EU legislator did not qualify the EU ETS itself as being based on 'provisions primarily of a fiscal nature'. It thus implemented the scheme following the ordinary legislative procedure according to Article 192.1 TFEU. This is not entirely uncontentious: the European Court of Justice (ECJ) has not yet ruled explicitly on the matter whether or not the EU ETS was based on the right legal basis. In the scholarly literature, it is sometimes claimed that the EU ETS should have been based on Article 192.2 TFEU, as the financial obligation

imposed under this scheme is comparable to a tax and the revenues generated are given to the national budgets.⁴²

Nevertheless, it can be stated with some degree of certainty from the ECJ's case law that the EU ETS is not based on 'provisions primarily of a fiscal nature'. This is because the Court has rendered several judgments on the EU ETS,⁴³ without even mentioning the question of the right legal basis. Had it held doubts in that respect, it could have considered the validity of the Directive in its jurisprudence.⁴⁴

Moreover, the judgment in the *ATAA* case⁴⁵ also points in this direction. In the case, the ECJ had to decide, among other questions, whether the extension of the EU ETS to international aviation violated the Open Skies Agreement.⁴⁶ Under these provisions, the EU is obliged to exempt the fuel load from taxes, duties, fees and charges. The claimants argued that the obligation to surrender allowances per tonne of fuel consumed during flights constitutes a prohibited tax and charge under Articles 11.1 and 11.2(c) of the Open Skies Agreement, as the calculation of emissions which have to be covered by allowances is based on the fuel consumption and an emission factor. While it is true that the judgment focused on the inclusion of aviation in the EU ETS and was not rendered with regard to the right legal basis of EU ETS under European law, the reasoning of the Court can be applied *mutatis mutandis* to the question of the legal basis for the EU ETS as a whole.

⁴² See, e.g., F. Kirchhof and I. Kemmer, 'Einstimmigkeitserfordernis im Rat bei der Beschlussfassung über eine europäische Richtlinie zum Handel mit Treibhausgasemissionsberechtigungen', 11:5 *Europäisches Wirtschafts- und Steuerrecht* (2003), 217; C. Seiler, 'Kompetenz- und verfahrensrechtliche Maßstäbe europäischer Umweltabgaben', 45:1 *Europarecht* (2010), 67.

⁴³ ECJ, Cases C-503/07 P, *Saint-Gobain Glass Deutschland GmbH v. Commission of the European Communities*, [2008] ECR I-2217; C-148/14, *European Commission v. French Republic*, [2010] OJ C148/9; C-524/09, *Ville de Lyon v. Caisse des Dépôts et Consignations*, [2010] ECR I-12115; C-279/08 P, *European Commission v. Kingdom of the Netherlands*, [2011] ECR I-7714; C-366/10, *ATAA v. Secretary of State for Energy and Climate Change*, [2011] ECR I-13755; C-505/09 P, *European Commission v. Republic of Estonia*, ECLI:EU:C:2012:179; C-504/09 P, *Commission v. Poland*, ECLI:EU:C:2012:178; *Iberdrola, SA*, n. 3 above; C-267/11 P, *European Commission v. Republic of Latvia*, ECLI:EU:C:2013:624; C-425/13, *Commission v. Council*, ECLI:EU:C:2015:483; C-148/14, *Bundesrepublik Deutschland v. Nordzucker AG*, ECLI:EU:C:2015:287.

⁴⁴ ECJ, Case 62/76, *Strehl v. Nationaal Pensioenfonds voor Mijnwerkers*, [1977] ECR 211, at paragraphs 10ff. where the Court chose to consider the validity of the act the mere interpretation of which was requested.

⁴⁵ Case C-366/10, n. 43 above.

⁴⁶ Air Transport Agreement between the European Community and its Member States and the United States of America (Brussels/Washington, 25 and 30 April 2007; provisionally applied 30 March 2008), as amended by the Protocol to amend the Air Transport Agreement between the European Community and its Member States and the United States of America (Luxembourg, 24 June 2010; provisionally applied 24 June 2010).

⁴⁰ *Ibid.*, Articles 289.1 and 298.

⁴¹ According to TEU, n. 38 above, Article 16.4, a qualified majority requires at least 55% of the members of the Council, comprising at least 15 of them and representing Member States comprising at least 65% of the population of the Union.

The ECJ followed the opinion of Advocate General Kokott and denied that the extension of the EU ETS to international aviation amounted to a tax or a similar charge. It stated that:

unlike a duty, tax, fee or charge on fuel consumption, the scheme . . . , apart from the fact that it is not intended to generate revenue for the public authorities, does not in any way enable the establishment, applying a basis of assessment and a rate defined in advance, of an amount that must be payable per tonne of fuel consumed for all flights carried out in a calendar year.⁴⁷

Or in the clear words of Advocate General Kokott:

It would be unusual, to put it mildly, to describe as a charge or tax the purchase price paid for an emission allowance, which is based on supply and demand according to free market forces, notwithstanding the fact that the Member States do have a certain discretion regarding the use to be made of revenues generated.⁴⁸

The Court did not consider the requirements for a tax, charge or fee on (fuel) consumption to be fulfilled. First, there was no inseparable link between the quantity of fuel consumed and the amount of money payable. Although the Court saw a certain link between the consumption of fuel and the financial obligation imposed,⁴⁹ it refused to regard as inseparable the link 'between the quantity of fuel held or consumed by an aircraft and the pecuniary burden on the aircraft's operator in the context of the allowance trading scheme's operation'.⁵⁰ It reasoned that the financial obligation imposed on airlines was not set at a fixed level by governments, but determined by the market mechanism of the EU ETS, in particular the market price of allowances.⁵¹ Second, the financial obligation was not imposed in order to gener-

ate revenue for the public authorities.⁵² The imposition of a financial burden was not intended to generate revenues for the public authorities,⁵³ but to protect the environment by imposing costs on emissions and thereby incentivizing economic operators to reduce emissions at the lowest costs.⁵⁴

Accordingly, were the ECJ to rule on the question whether the EU ETS has been based on the right legal basis, the Court would most likely apply the same reasoning and conclude that it was based correctly on Article 192.1 TFEU. This is because the scheme is a market-based system, the financial obligation imposed thereunder is determined by supply and demand and it is not the primary intention of the scheme to generate revenues for the public budgets. Rather, the revenues are auxiliary to the scheme which incentivizes an efficient use of the natural resource of clean air.

Inclusion of Consumption as an Integral Part of the EU ETS

If the above analysis that the EU ETS could be based on Article 192.1 TFEU rather than Article 192.2 TFEU is correct, in our view, the same must be true for the inclusion of consumption. This link with respect to the legal basis is due to the fact that the inclusion of consumption would, as demonstrated in the following, form an integral part of the EU ETS that addresses the inherent problems of the system caused by free allocation as an anti-leakage measure. This is supported by a host of reasons: the purpose of the inclusion of consumption, the integration of imports in the EU ETS, the link to free allocation and its technical implementation.

The first and most important argument is provided by the aim of the inclusion of consumption, namely, restoring the second channel ('sending a price signal along the value chain'). As indicated above, the EU ETS provides two different measures to achieve emission reductions: in addition to securing upstream production efficiency,⁵⁵ it also seeks to send a price signal along the value chain in order to incentivize substitution for lower-carbon products and to promote innovation.⁵⁶ Although the latter is not expressly mentioned by the EU ETS Directive, it is, according to the statement of

⁴⁷ Case C-366/10, n. 43 above, at paragraph 143. On this see also M. Gehring, 'Case Note: Air Transport Association of America v. Energy Secretary: Clarifying Direct Effect and Providing Guidance for Future Instrument Design for a Green Economy in the European Union', 21:2 *Review of European Community and International Environmental Law* (2012), 149, at 153; J. Korn, 'Von "open skies" und "green shipping" – Zur Bedeutung des Urteils über die Einbeziehung des Luftverkehrs in den Emissionshandel für das europäische Emissionsreduzierungsvorhaben in der Hochseeschifffahrt', 34:11 *Natur und Recht* (2012), 759, at 761ff. Of a different opinion: A. Gattini, 'Between Splendid Isolation and Tentative Imperialism: The EU's Extension of its Emissions Trading Scheme to International Aviation and the ECJ's Judgment in the ATA Case', 61:4 *International and Comparative Law Quarterly* (2012), 977, at 988; B. Havel and J. Mulligan, 'The Triumph of Politics: Reflections on the Judgement of the Court of Justice of the European Union Validating the Inclusion of Non-EU Airlines in the Emissions Trading Scheme', 37:1 *Air and Space Law* (2012), 3, at 30ff.; B. Mayer, 'Case C-366/10, *Air Transport Association of America and Others v. Secretary of State for Energy and Climate Change*, Judgment of the Court of Justice (Grand Chamber) of 21 December 2011', 49:3 *Common Market Law Review* (2008), 1113, at 1135ff.

⁴⁸ Case C-366/10, n. 43 above, Opinion of AG Kokott delivered on 6 October 2011, at paragraphs 216 and 227.

⁴⁹ Case C-366/10, n. 43 above, at paragraph 141.

⁵⁰ *Ibid.*, at paragraph 142.

⁵¹ See also B. Havel and J. Mulligan, n. 47 above, at 29ff.; S. Bogojevic, 'Analysis – Legalising Environmental Leadership: A

Comment on the ECJ's Ruling in C-366/10 on the Inclusion of Aviation in the EU Emissions Trading Scheme', 24:2 *Journal of Environmental Law* (2012), 345, at 354.

⁵² See B. Mayer, n. 47 above, at 1134.

⁵³ Case C-366/10, n. 43 above, at paragraph 143.

⁵⁴ *Ibid.*, at paragraphs 139ff. See also S. Bogojevic, n. 51 above, at 353ff.

⁵⁵ See M. Grubb *et al.*, n. 4 above, at Chapters 6 and 7.

⁵⁶ Opinion of AG Kokott, *Iberdrola, SA*, n. 5 above, at paragraph 70; Commission of the European Communities, n. 5 above, at paragraph 7.3; R. Ismer, n. 5 above, at 104.

Advocate General Kokott in *Iberdrola, SA*,⁵⁷ ‘consistent with the logic of the market mechanism created by it’.⁵⁸

In this case, the ECJ had to decide whether a Spanish levy on electricity producers was compatible with the obligation under Article 10 of Directive 2003/87 to allocate the first 95% and then 90%⁵⁹ of allowances free of charge. The levy was intended to absorb windfall profits created by the integration of opportunity costs in the electricity price for freely allocated allowances. The claimants argued that the levy ‘neutralises the “free of charge” nature of emission allowances’.⁶⁰ The ECJ rejected the claim. While the Court reasoned that the objective of the EU ETS was the reduction of emissions in a cost-effective and economically efficient manner⁶¹ rather than a pass-through of carbon costs, it did not reject that one way to achieve the aim of emission reductions was the reflection of carbon costs in the consumption price. The Court thereby followed the view of Advocate General Kokott, who had stated that the argument that the EU ETS aims to integrate carbon prices into consumption prices⁶²

is essentially well-founded. If the opportunity costs of the allowances are integrated into consumer prices, that price signal gives consumers an additional incentive to consume less electricity and thus to help to reduce greenhouse gas emissions. Although Directive 2003/87 does not expressly mention this incentive for final consumers, it is consistent with the logic of the market mechanism created by it. That mechanism is intended to put a price on environmental pollution so that those costs are included in the decision making of *all relevant actors*.⁶³

It follows that even if the EU ETS may not aim to reflect carbon costs in the consumption price, such reflection may nevertheless contribute to its objective.

In the same judgment, the ECJ had shown concerns regarding free allocation. More specifically, it stated that free allocation

was not intended as a way of granting subsidies to the producers concerned, but of reducing the economic impact of the immediate and unilateral introduction by the European Union of an emissions allowance market, by preventing a loss of competitiveness in certain production sectors covered by that directive.⁶⁴

The ECJ further noted that the problem of windfall profits would be eliminated in the future, as from 2013 onwards, ‘the emission allowances are to be allocated by means of a full auctioning mechanism’⁶⁵ and that

free allocation itself is not directly related to the environmental objective of reducing emissions.⁶⁶ It can be inferred that any measure which would do more justice to the aims of the EU ETS is preferential compared to free allowance allocation. This would exactly be the case for the inclusion of consumption. The scheme would restore the carbon price signal for consumers of goods from these sectors and, as all production along the value chain would be pursued with the perspective of service and cost delivered to the final consumer, the inclusion of consumption would reinstate the carbon price signal and resulting incentives for mitigation for the entire value chain. It would thus facilitate effective leakage protection while ensuring the integrity of the EU ETS and its aims.⁶⁷

The second argument is that the integration of imports under the inclusion of consumption takes up and further develops the possibility of creating the obligation to surrender allowances for imports as already provided for in Article 10b of the EU ETS Directive.⁶⁸ This measure ‘could be introduced with a view to putting installations from the Community which are at significant risk of carbon leakage and those from third countries on a comparable footing’.⁶⁹ The inclusion of consumption – which takes a similar, but slightly different route – would even better accomplish this objective for two reasons.

First, its effects would not be limited to goods consumed in the EU. Rather, the goods produced in the EU held under a duty suspension arrangement prior to exportation would be relieved from the charge. These goods could thus compete on a comparable footing outside the EU, which is something that the mere inclusion of imports under Article 10b of the EU ETS Directive would not allow.

Second, the number of EU ETS allowances available on the carbon market would be reduced only by the net inflow of carbon-intensive commodities. As under the inclusion of imports, there would be a direct link between the inclusion of consumption and the EU ETS, as the funds raised would be partially employed for the *acquisition of allowances* for net imports, if any, on the market. The fact that the revenue raised under the inclusion of consumption is not fully used for the purchase of allowances is again motivated by reasons internal to the EU ETS: otherwise, there would not only be a potential for double counting of emissions, but also an unclear impact upon scarcity, which through a fixed cap translates into an unclear price impact and thus to

⁵⁷ *Iberdrola, SA*, n. 3 above.

⁵⁸ Opinion of AG Kokott, *Iberdrola, SA*, n. 5 above, at paragraph 71.

⁵⁹ Directive 2003/87/EC, n. 1 above, Article 10.

⁶⁰ *Iberdrola, SA*, n. 3 above, at paragraph 19.

⁶¹ *Ibid.*, at paragraph 56.

⁶² Opinion of AG Kokott, *Iberdrola, SA*, n. 5 above, at paragraph 69.

⁶³ *Ibid.*, at paragraphs 70ff. (emphasis added).

⁶⁴ *Iberdrola, SA*, n. 3 above, at paragraph 39.

⁶⁵ *Ibid.*, at paragraph 40.

⁶⁶ *Ibid.*, at paragraph 45.

⁶⁷ The EU ETS promotes reductions of greenhouse gas emissions in a cost-effective and economically efficient manner.

⁶⁸ Directive 2003/87/EC as amended by Directive 2009/29/EC, n. 1 above; see also Directive 2009/29/EC, n. 1 above, recital 25.

⁶⁹ Directive 2009/29/EC, n. 1 above, recital 25.

increased risk for participants. This means that the inclusion of consumption would limit itself to reversing the financial impact of the free allocation without affecting the number of allowances available on the market beyond what is necessary to correct for locational shifts of production patterns to serve European consumption and address the scarcity of allowances.

The third argument is based on the link of the proposed inclusion of consumption to the allowance price and to free allocation: the fact that the charge under the inclusion of consumption would be linked to the price of EU ETS allowances on the carbon markets underlines the close integration of the proposal with the current EU ETS. The inclusion of consumption would also be closely linked to the rules on free allocation. Technically, the same benchmark that is used for determining free allocation is also applicable for calculating the charge. There would also be a substantive connection: free allowance allocation assists sectors that would otherwise face the risk of carbon leakage. Imposing a charge on consumption coupled with output-based free allocation would not only maintain leakage protection, but – compliant with WTO law – claw back the free allocation once the good is released for consumption in the EU. It would align the overall burden to be borne by the consumer with that under full auctioning, which is to ‘be the basic principle for allocation, as it is the simplest, and generally considered to be the most economically efficient, system’.⁷⁰

The use of funds not needed for purchasing allowances further shows a close connection to the general EU ETS. The (most likely very large⁷¹) share of the funds that would not be necessary to cover net imports would not go to the general government budget, but would be earmarked for climate purposes as defined in the EU ETS Directive for auction revenue from EU ETS generally.⁷² Thus, it would correct some of the climate funding problems resulting from free allocation. Free allocation means that these allowances cannot be auctioned and that less money is available for climate purposes than under full auctioning. Using the remainder of the money raised through the inclusion of consumption for such purposes would secure the revenue for mitigation and thus lead also with respect to funding to a situation resembling full auctioning.

⁷⁰ *Ibid.*, recital 15.

⁷¹ The charge becomes due for every import. By contrast, the funds are used to purchase allowances only for net imports, i.e., after deducting exports. Exports in carbon-intensive goods are significant meaning that imports are far bigger than net imports (i.e., imports minus exports).

⁷² Directive 2003/87/EC as amended by Directive 2009/29/EC, n. 1 above, Article 10.3.

Against this background, it does not constitute a convincing counter-argument that the desired financial impact upon the consumers could also be reached by obliging them to surrender a number of allowances, which would reflect the carbon content of the goods they consumed. This would at least in theory establish an even closer link to the EU ETS than the inclusion of consumption. It would, however, mean that consumers or retailers (or any other person releasing the good for consumption, such as importers operating outside a duty suspension arrangement) would have to be accommodated in the trading infrastructure of the EU ETS. This would create significant compliance costs on their part. There would, moreover, be an increase in the number of small and potentially somewhat ill-informed traders, which would threaten to reduce the efficiency of carbon markets. The fact that the desired financial impact on consumers takes the form of an inclusion of consumption rather than direct consumer participation in the EU ETS is thus not motivated by the desire to raise revenue, but by objectives internal to the EU ETS.

All this means that the inclusion of consumption would form an integral part of the EU ETS as it would: pursue the same objectives (reducing emissions); use the same means (incentivizing an efficient use of carbon-intensive commodities by cost allocation); yield the same results as full auctioning, which is the basic principle of allocation under the EU ETS; and put domestic and foreign products on an equal footing – just as foreseen by the EU ETS Directive. In addition, the inclusion of consumption would remedy the current inefficiencies of the EU ETS. The above reasoning that the EU ETS was not based on ‘provisions primarily of a fiscal nature’ in the sense of Article 192.2(a) TFEU and thus did not require unanimity in the Council, can therefore also be applied to the inclusion of consumption. Unanimity would not be necessary for adopting the inclusion of consumption. Instead, the qualified majority under Article 192.1 TFEU would be sufficient.

NOT ‘PROVISIONS PRIMARILY OF A FISCAL NATURE’ EVEN IF INCLUSION OF CONSUMPTION HAS TO BE ASSESSED SEPARATELY

Even if, contrary to what has just been set out, the inclusion of consumption could not be considered an integral part of the EU ETS, it would arguably still not be based upon ‘provisions primarily of a fiscal nature’ in the sense of Article 192.2(a) TFEU. While there is no pertinent case law on Article 192.2(a) TFEU that could shed light on the meaning of the term ‘provisions primarily of a fiscal nature’, the term may only include charges which are comparable with taxes in the narrow

sense but not a parafiscal charge⁷³ like the one imposed under the inclusion of consumption.

The Term 'Fiscal' is Non-decisive

The term 'fiscal' must be considered to be non-decisive, since it could be given several different interpretations. One could be tempted to argue that with, i.e., Article 113 TFEU speaking explicitly of taxes, the term 'fiscal' in Article 192.2(a) TFEU must cover more than mere taxes. The provision could then embrace instruments that either have a similar effect to that of a tax or are comparable with a tax in the narrow sense. Yet a closer look at the versions of the text in the other Treaty languages reveals ambiguity. Most narrowly, the German wording of Article 192.2(a) TFEU (as well as that in a sizeable number of other languages⁷⁴) merely refer to '*Vorschriften überwiegend steuerlicher Art*'. The term '*Steuer*' (German for 'tax') is legally defined in the Fiscal Code of Germany as 'payments of money, other than payments made in consideration of the performance of a particular activity, which are collected by a public body for the purpose of raising revenue and imposed by the body on all persons to whom the characteristics on which the law bases liability for payment apply'.⁷⁵ The German scholarly literature thus considers Article 192.2(a) TFEU to be limited to taxes only.⁷⁶ By contrast, most other languages use an expression that is at least at first glance similar to the English expression. Yet even where this is the case, other considerations cannot be neglected: the French doctrine, e.g., has traditionally

drawn a clear distinction between fiscal charges on the one hand and parafiscal charges on the other.⁷⁷

Given the principle of linguistic equality,⁷⁸ neither the German wording nor any other language version which implies a wider understanding can be considered as decisive. Instead, the different language versions of the text 'must be given a uniform interpretation and hence in the case of divergence between the versions the provision in question must be interpreted by reference to the purpose and general scheme of the rules of which it forms part'.⁷⁹

Narrow Interpretation for Exceptions

The point of departure for the interpretation of the term 'provisions primarily of a fiscal nature' in Article 192.2(a) TFEU has to be that the provision is to be given a narrow interpretation as it represents an exception to the general rule of Article 192.1 TFEU. Admittedly, one may doubt whether the Roman law interpretative rule of '*singularia non sunt extendenda*'⁸⁰ (exceptions are not to be extended) can be relied upon when interpreting European law.⁸¹ Nevertheless, the ECJ has often referred to such a rule,⁸² at least where the purpose of the provision is not in conflict with the narrow interpretation.

⁷³ While taxes are generally paid to national budgets and used to cover general public expenses, parafiscal charges are assigned to a separate body of public law. The money raised is earmarked and used for certain policy objectives.

⁷⁴ See the Estonian ('maksusätteid'), Greek ('φορολογικού'), Hungarian ('adózási'), Slovenian ('davčne') and Swedish ('skattekaraktär') versions.

⁷⁵ Fiscal Code of Germany (*Abgabenordnung*), Section 3 (translation provided by the Language Service of the German Federal Ministry of Finance). For similar definitions of 'tax', see Public Finances General Directorate Tax Policy Directorate, *The French Tax System* (situation as at 31 July 2011), at 7 ('[t]axes are payments imposed on individuals and legal entities according to their ability to pay without any specific consideration in return in order to cover public spending and achieve the economic and social objectives set by the government'), as well as R. Ismer and A. Blank, 'Article 2. Taxes Covered', in: E. Reimer and A. Rust (eds.), *Klaus Vogel on Double Taxation Conventions* (Kluwer Law, 2015), 143, at paragraphs 8ff.

⁷⁶ C. Calliess, 'AEUV Artikel 192', in: C. Calliess and M. Ruffert (eds.), *EU/VAEUV: Das Verfassungsrecht der Europäischen Union mit Europäischer Grundrechtecharta Kommentar* (C.H. Beck, 2011), 1939, at paragraph 29; M. Nettesheim, 'AEUV Artikel 192', in: E. Grabitz, M. Hilf and M. Nettesheim (eds.), *Das Recht der Europäischen Union* (C.H. Beck, 2014), at paragraphs 77ff. A different view is held by C. Ohler, 'Die Finanzierung des IASB durch EG-Sonderabgaben', 27:22 *Europäische Zeitschrift für Wirtschaftsrecht* (2006), 679, who focuses on the parallel provision of Article 194.3 TFEU, and rightly points to the French and English versions of the Treaty.

⁷⁷ See Order No 59-2 of 2 January 1959 (*Ordonnance n° 59-2 du 2 janvier 1959 portant loi organique relative aux lois de finances*), Article 4. Repealed by Organic Law No. 2001-692 of 1 August 2001 (*Loi organique n° 2001-692 du 1 août 2001 relative aux lois de finances*), Article 67.

⁷⁸ TEU, n. 38 above, Article 55; see K. Lenaerts and J. Gutiérrez-Fons, *To Say What the Law of the EU Is: Methods of Interpretation and the European Court of Justice* (Academy of European Law, 2013), at 11. A narrow interpretation that is solely based on the wording of one language version of the treaties barely satisfies the principle of linguistic equality, in particular if Member States have a different understanding of legal terms. See K. Meßerschmidt, *Europäisches Umweltrecht* (C.H. Beck, 2011), at 109. Hence, the ECJ emphasizes the necessity of an autonomous and uniform interpretation of the European treaties to ensure a uniform application of the law of the European Union. See ECJ, Cases C-327/82, *Ekro v. Produktschap voor Vee en Vlees*, [1984] ECR 107, at paragraph 11; C-287/98, *State of the Grand Duchy of Luxembourg v. Linster and Others*, [2000] ECR I-6917, at paragraph 43; and C-357/98, *The Queen v. Secretary of State for the Home Department*, [2000] ECR I-9285, at paragraph 26.

⁷⁹ ECJ, Case C-30/77, *Regina v. Pierre Bouchereau*, [1977] ECR 1999, at paragraph 14; see also ECJ, Cases C-803/79, *Gérard Roudolff*, [1980] ECR 2016, at paragraph 7; C-449/93, *Rockfon*, [1995] ECR I-4291, at paragraph 28; C-236/97, *Skatteministeriet v. Codan*, [1998] ECR I-8679, at paragraph 28; C-36/98, *Kingdom of Spain v. Council*, [2001] ECR I-779, at paragraph 49.

⁸⁰ Dig. 40.5.23.3 and Dig. 41.2.44.1 (Papinian).

⁸¹ See T. Schilling, 'Singularia non sunt extendenda: Dis Auslegung der Ausnahmen in der Rechtsprechung des EuGH', 31:1 *Europarecht* (1996), 44.

⁸² See, e.g., ECJ, Cases C-16/69, *Commission v. Government of the Italian Republic*, [1969] ECR 377, at paragraphs 5ff.; C-176/73, *Claudette Van Belle v. Council*, [1974] ECR 1361, at paragraphs 21–24; C-229/83, *Leclerc v. Au blé vert*, [1985] ECR 1, at paragraph 30. See also the references in T. Schilling, n. 81 above, at 47ff.

More importantly, the ECJ has in the *Danube* case⁸³ spoken out in favour of a narrow interpretation of Article 130s of the European Community (EC) Treaty,⁸⁴ the slightly differently worded predecessor of Article 192.2(b) TFEU. The case revolved around the action of Spain against the decision by the Council through which it approved on behalf of the Community the Convention on Cooperation for the Protection and Sustainable Use of the River Danube.⁸⁵ According to Article 217.8 TFEU (then Article 228.2 EC Treaty), the procedure applicable to the conclusion of such an external agreement mirrors the procedural requirements for internal rules: if the agreement relates to a matter for which unanimity is required for the adoption of internal rules, the Council is to act unanimously. In other cases, it acts by a qualified majority. Spain pleaded that the legal basis adopted was inappropriate as the Convention dealt with the management of water resources so that unanimity under the then Article 130.2(b) EC Treaty would have been required. The ECJ rejected that plea and ruled that Article 130.2(b) EC Treaty was limited to quantitative water management measures, whereas qualitative measures fell under the general rule of Article 130s.1 EC Treaty. The ECJ did not explicitly refer to the *singularia* rule. Nevertheless, it opted for a narrow interpretation of a term that was structurally parallel to the term ‘provisions primarily of a fiscal nature’. This suggests that the ECJ would tend to choose a narrow interpretation also with respect to the term ‘provisions primarily of a fiscal nature’ under Article 192.2 TFEU.

Systemic Interpretation: Inclusion of Consumption not (Primarily) of a Fiscal Nature

Greater clarity can indeed be reached by taking into account the context of the term ‘primarily of a fiscal nature’ in Article 192.2(a) TFEU. The term ‘fiscal nature’ has to be construed so as to go beyond taxes in the narrow sense as, otherwise, the legislator would simply have used the term ‘tax’ as in Article 113 TFEU. Nevertheless, a careful analysis of the three instances where the TFEU uses this term – namely, in the second sentence of Article 30, Articles 192.2(a) and 194.3 TFEU – shows that the inclusion of consumption, even when it could not be considered an integral part of the EU ETS, would not be based upon ‘provisions primarily of a fiscal nature’.

To understand the meaning of the term ‘fiscal nature’ in the second sentence of Article 30 TFEU, the second

sentence has to be read in conjunction with the first. Article 30 TFEU reads as follows: ‘Customs duties on imports and exports and charges having equivalent effect shall be prohibited between Member States. This prohibition shall also apply to customs duties of a fiscal nature.’ Accordingly, there has to be a difference between customs imposed in order to control the trade flows between Member States to protect the domestic market and customs which are imposed to raise government revenue.⁸⁶ The distinction between the two is based upon the purpose of the measure. Customs designed mainly to raise revenue for the public budget are of a fiscal nature, whereas this is not the case where the primary purpose is to induce certain behaviour and the raising of revenues is simply accessory to the mechanism.

Article 194.3, just like Article 192.2(a) TFEU, requires unanimity in the Council. Both provisions can be understood as addressing Member States’ sovereignty concerns. The same is true of other instances where the word ‘fiscal’ is used in the TFEU. Article 114.2 exempts fiscal provisions from the scope of the provision that allows the adoption of measures regarding the establishment and functioning of the internal market. The ECJ has ruled that the term is neither confined to taxes in the narrow sense nor to substantive tax rules, but also covers other charges and procedural provisions.⁸⁷ The ECJ’s ruling in *Schraeder v. Hauptzollamt Gronau*⁸⁸ concerning the European Economic Community’s (EEC) own resources demonstrates that such sovereignty nevertheless is limited. In that case, the claimant (Schraeder) wanted to challenge a levy on cereals which was imposed as an intervention measure designed to stabilize agricultural markets by restricting cereal production. Schraeder argued that the levy was a financial charge and thus should have been based on the former Article 201 EEC Treaty, which would have required unanimity in the Council. The ECJ, however, held that the objective of this policy measure had to be the decisive criterion and that Article 201 EEC Treaty was not applicable ‘merely because the measure entails the collection of revenues’.⁸⁹ Hence, the levy was correctly based on the former Article 43 EEC Treaty,⁹⁰ which did not require unanimity in the Council. This reasoning may be transferred to the inclusion of consumption: although the inclusion of consumption might entail the collection of revenue, its objective would clearly lie in securing leakage protection in a

⁸³ Case C-36/98, n. 79 above; see also K. Meßerschmidt, n. 78 above, at 109.

⁸⁴ Treaty on European Union, together with the complete text of the treaty establishing the European Community, [1992] OJ C 244/1.

⁸⁵ Council Decision of 24 November 1997 Concerning the Conclusion of the Convention on Cooperation for the Protection and Sustainable Use of the River Danube, [1997] OJ L342/19.

⁸⁶ J.P. Terhechte, ‘Artikel 30 AEUV’, in: J. Schwarze (ed.), *EU-Kommentar* (Helbing Lichtenhahn Verlag, 2012), 557, at paragraphs 7ff.

⁸⁷ ECJ, Case C-388/01, *Commission v. Council*, [2004] ECR I-4852, at paragraph 67.

⁸⁸ ECJ, Case C-265/87, *Schraeder v. Hauptzollamt Gronau*, [1989] ECR 2240.

⁸⁹ *Ibid.*, at paragraph 11.

⁹⁰ *Ibid.*, at paragraph 12.

WTO-compatible way whilst avoiding the detrimental effects of unfettered free allocation.

A similar approach has been applied by the ECJ more generally to the determination of the proper legal basis of policy measures. This means that the choice of legal basis is determined in particular by the aim and the content of a measure.⁹¹ In practice, the ECJ then has recourse to the main (subjective) purpose of a policy measure.⁹² Accordingly, the ECJ would look at the purpose of a measure to decide whether this measure is comparable with a tax in the narrow sense. A similar approach was adopted by the ECJ in the *ATAA* case. Instead of qualifying the EU ETS according to the means employed (i.e., a financial obligation imposed on aircraft operators), the ECJ qualified the EU ETS based on the objective pursued. The objectives of a measure thus override the means employed to reach these objectives. In the case of inclusion of consumption, the charge would imply payments to the State, which would, however, be accessory to the mechanism and not an end in itself. As the main objectives of the inclusion of consumption are to reduce emissions and to curb leakage, the mechanism would be qualified as not being of a fiscal nature.

Moreover, it appears noteworthy that the ECJ⁹³ has repeatedly distinguished taxes (i.e., fiscal instruments) and parafiscal charges. The main difference is that parafiscal charges are not paid into the national budget, but are assigned to a separate body of public law. Revenue raised then cannot be used for covering the general public expenses of public authorities. The fact that the revenue from the inclusion of consumption is given to a special trust fund rather than to the general government budget thus also supports the view that no unanimity is required.

Further support for the view that the inclusion of consumption does not fall within the ambit of Article 192.2(a) TFEU is lent by the word ‘*primarily*’, which

relates to fiscal nature. It shows that the mere fact that revenue is raised is not sufficient as long as this is not the primary purpose.⁹⁴

This result is not changed by recent developments with respect to the term ‘State resources’ under EU State aid rules. Admittedly, the term is no longer confined to advantages granted from public funds, but also comprises separate private funds that are controlled by the government.⁹⁵ As shown by the recent infringement proceedings against Germany regarding feed-in tariffs for renewable energy,⁹⁶ this implies in particular that exemptions for energy-intensive industries from the levy financing such mechanisms are no longer off-limits for State aid control.⁹⁷ Nevertheless, this expansive view cannot be transferred to Article 192.2(a) TFEU. To ensure their effectiveness, the State aid provisions have to be given a wide interpretation so as to limit collusion between Member States and enterprises. By contrast, there is no such overriding purpose of Article 192.2(a) TFEU, which addresses Member States’ sovereignty concerns⁹⁸ and thus effectively limits the scope for EU activity.

CONCLUSION

Given the deficiencies of free allocation and border carbon adjustments, the inclusion of consumption has emerged as a solution to the problem of carbon leakage. This article has demonstrated that the inclusion of consumption in the EU ETS would be considered part of EU environmental regulation and as such requires qualified majority rather than unanimity voting in the Council under Article 192.2(a) TFEU, as it would not constitute a measure of a primarily fiscal nature. This is because the EU ETS itself did not necessitate unanimity as it was not based on ‘provisions primarily of a fiscal nature’ in the sense of that provision. The same would be true for the inclusion of consumption, as it would constitute a mere ancillary extension to the EU ETS for several reasons. First, the aim of the inclusion of consumption would help to send a price signal along the

⁹¹ ECJ, Cases C-45/86, *Commission v. Council*, [1987] ECR 1493, at paragraph 11; C-300/89, *Commission v. Council*, [1991] ECR I-2895, at paragraph 10; C-155/91, *Commission v. Council*, [1993] ECR I-939, at paragraph 7; C-271/94, *Parliament v. Council*, [1996] ECR I-1689, at paragraph 14; and C-164/97 and C-165/97, *Parliament v. Council*, [1999] ECR I-1139, at paragraph 12.

⁹² Case C-155/91, n. 91 above; ECJ, Cases C-84/94, *UK v. Council*, [1996] ECR I-5755, at paragraph 21; C-377/98, *Netherlands v. Parliament and Council*, [2001] ECR I-7079, at paragraph 27.

⁹³ ECJ, Cases C-94/74, *ENCC*, [1975] ECR 699, at paragraphs 8ff.; C-77/76, *Fratelli Cucci & Avez*, [1977] ECR 988, at paragraph 1001; Joined Cases C-78 and C-83/90, *Compagnie Commerciale de l'Ouest and Others v. Receveur Principal des Douanes de La Pallice Port*, [1992] ECR I-1873, at paragraphs 26–29, C-72/92, *Herbert Scharbatke v. Germany*, [1993] ECR I-5509, at paragraphs 9ff.

⁹⁴ Of the same opinion: P. Davies, *European Union Environmental Law: An Introduction to Key Selected Issues* (Ashgate, 2004), at 14; L. Krämer, *EU Environmental Law* (Sweet & Maxwell, 2011), at 82; J.H. Jans and H.H.B. Vedder, *European Environmental Law: After Lisbon* (Europa Law, 2012), at 60.

⁹⁵ ECJ, Case C-206/06, *Essent*, [2008] ECR I-5947, at paragraph 66; and Case C-262/12, *Vent de Colère*, ECLI:EU:C:2013:851, at paragraphs 25 and 37.

⁹⁶ European Commission, State Aid SA.33995 (2013/C) (ex 2013/NN) – Germany – Support for Renewable Electricity and Reduced EEG-surcharge for Energy-intensive Users (18 December 2013), C(2013) 4424 final.

⁹⁷ Cf. R. Ismer and A. Karch, ‘Das EEG im Konflikt mit dem Unionsrecht: Die Begünstigung der stromintensiven Industrie als unzulässige Beihilfe’, 24:10 *Zeitschrift für Umweltrecht* (2013), 526, at 526.

⁹⁸ C. Calliess, n. 76 above, at paragraphs 28f.

value chain, which must be a key aim of the EU ETS if it is to contribute to fully exhaust the potential for emission reductions. Second, using a charge rather than creating the obligation of retailers or consumers to surrender allowances would be motivated by ease of administration concerns rather than by the desire to raise revenue. Third, the acquisition of allowances for imports is already provided for in the current EU emissions trading Directive as a measure to address leakage. Fourth, the fact that the earmarking of funds for the acquisition of allowances would only cover net imports can be explained by reasons intrinsic to the EU ETS. Fifth, the proposed usage of funds also shows a close connection to the general EU ETS. Finally, the amount to be paid by the chargeable person would be closely linked to the EU ETS as it would depend upon: (i) the market price of EU ETS allowances; and (ii) the same benchmark. Moreover, even if the inclusion of consumption could not be considered an integral part of the EU ETS, Article 192.2(a) TFEU would still not apply. While the wording of the provision is unclear and differs between linguistic versions, its purpose and its

context reveal that the inclusion of consumption would not, or at least not primarily, be of a fiscal nature. All this means that from an EU law perspective, a solution to the leakage problems that preserves the integrity of the EU ETS and its aims is well within the realm of feasible measures.

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The authors wish to thank William Acworth, Angus Johnston, Klaus Meßerschmidt and Karsten Neuhoff as well as two anonymous referees for valuable comments. The usual caveat applies.