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# UK Indirect Tax Conference 2015

## Environmental taxes

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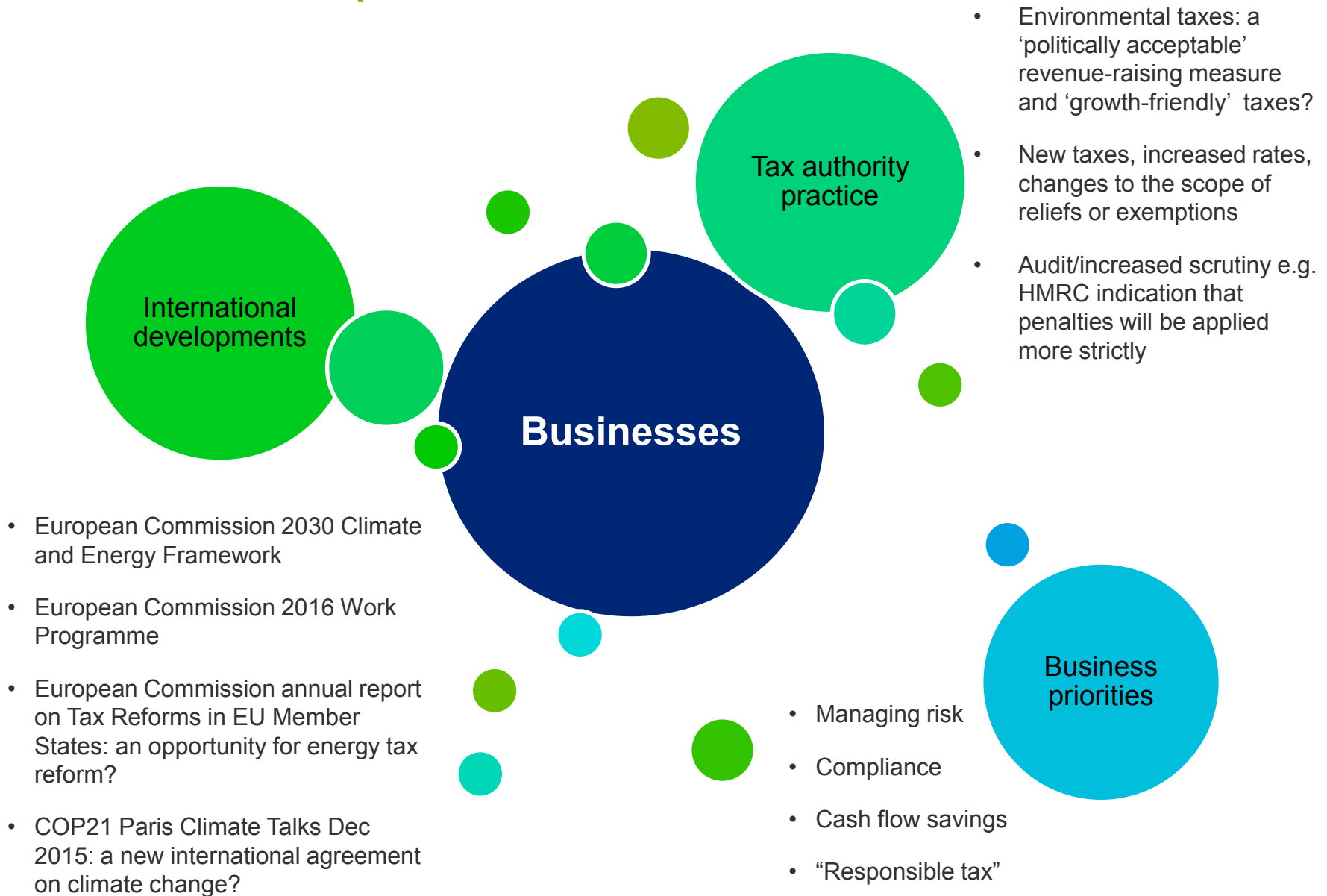


# Agenda

- Why does effective management of environmental taxes matter?
- Policy updates
- News and developments: UK and EU
- Case studies
- Q&A

# Why does effective management of environmental taxes matter?

# The landscape



# What is your strategy?

- Do you know how much environmental tax you pay in the UK?
- What is your approach to managing environmental taxes?
- How does your approach tie in with the overall tax strategy and the aims of your business?
- Should your approach factor in customer perception, the corporate sustainability agenda, reducing energy costs and increasing overall energy efficiency?
- Is there a case for you to engage in consultations with governments and key decision makers?
- Which part of the business adopts responsibility for issues of energy/environmental policy?
- Do you have the processes in place to react to change?

# Policy updates

**UK**

# Background: the current UK landscape

Current UK tax and legislative framework is complex, with a number of interacting and overlapping measures

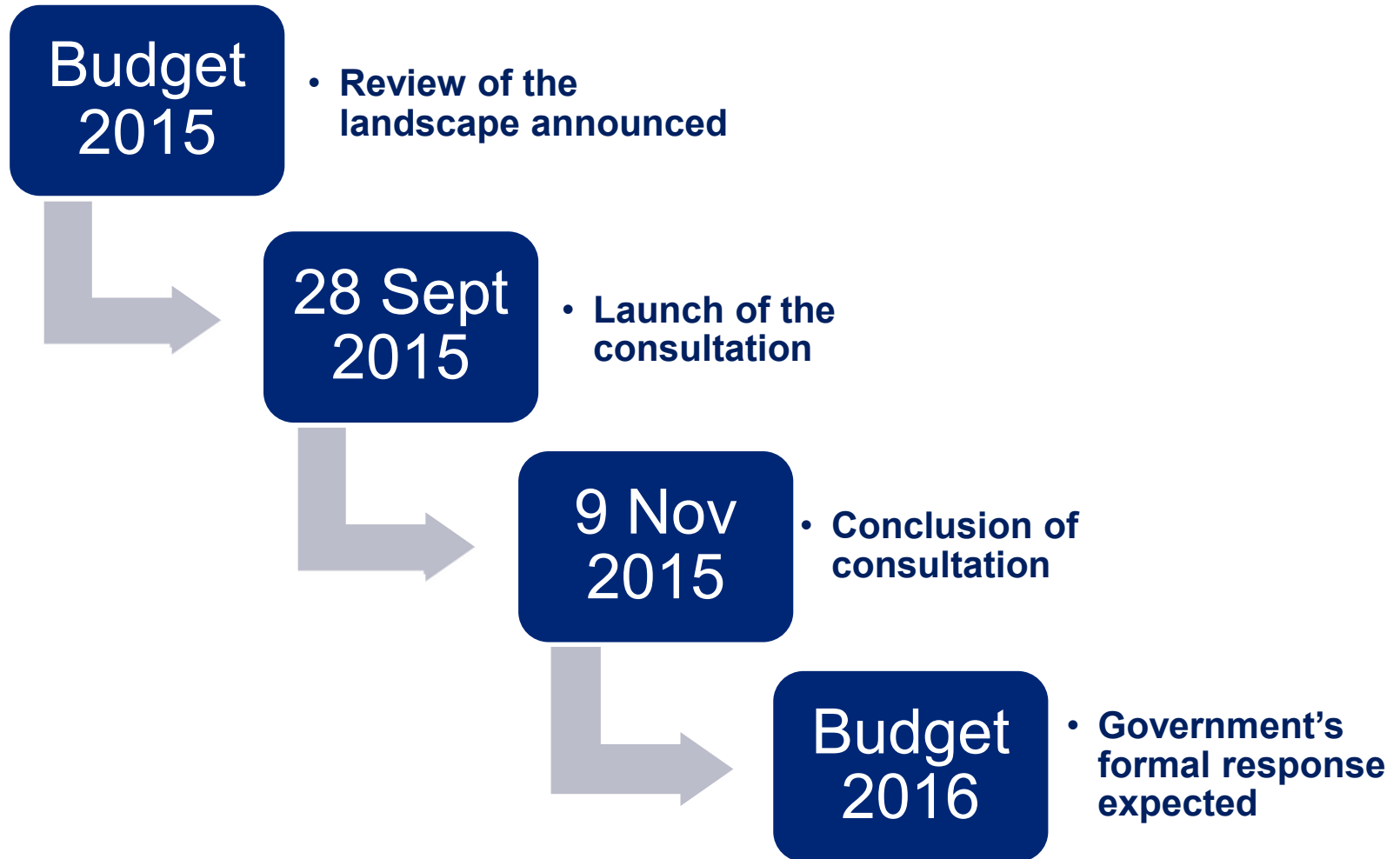
Instances of unexpected changes to policy

A need for a clear policy objective and simplification of the tax and regulatory framework

The CIOT called on the Government to put in place “an Environmental Tax Framework, or roadmap, for the rest of the Parliament... Businesses and consumers need certainty and clarity on these measures.”



# Reforming the business energy efficiency tax landscape: HMT and DECC consultation



# Reporting proposal

**To develop a single reporting framework which incorporates the most effective elements from the range of reporting schemes and delivers a significant net reduction in compliance costs associated with reporting schemes.**

General consensus: the overall aim of simplifying the landscape and moving to a single tax and single reporting framework is positive.

Issues to consider:

- keeping energy efficiency on the boardroom agenda;
- reporting frequency, format, benchmarking;
- linking reporting to incentives.

# Taxes and price signals proposal

**To move towards a single tax by abolishing the CRC and moving the revenue raising element into a single business energy consumption tax based on the CCL. The government is open to views as to the balance of tax costs across fuels, where proposals can better deliver carbon reduction potential.**

## Considerations:

- A clear objective;
- A roadmap of future changes;
- Simple for businesses and government to implement and manage;
- The balance of taxation between electricity and gas;
- Creating a level playing field between businesses in the same sector.

# Protecting the competitiveness of energy intensive industries proposal

**The government is open to considering options for new incentives in line with its overall objectives. Proposals would need to be funded through increases in tax to support fiscal consolidation objectives. Proposals would also need to be simple, meet strict value for money criteria and be more effective than other options.**

Considerations:

- HMT accept the need to protect energy intensive industries (EII);
- Should there be different incentives/measures applicable to different types of business (small, medium, large)?;
- Implications of the dual purpose of CCAs – protect EII and promote energy efficiency;
- Potential changes to CCA regime could lead to increased tax costs if current industry sectors are no longer covered under the new regime.

# Europe

# European Commission programmes

## 2030 climate and energy framework

Three key targets for the year 2030:

1. At least 40% cuts in greenhouse gas emissions (from 1990 levels)
2. At least 27% share for renewable energy
3. At least 27% improvement in energy efficiency

## Work Programme 2016

Objective: “A resilient energy union with a forward-looking climate change policy”

The Work Programme adopts key principles set out in the Energy Union Package, including actions relating to:

- Energy security
- Energy efficiency
- Emissions reduction

# News and developments

**UK**



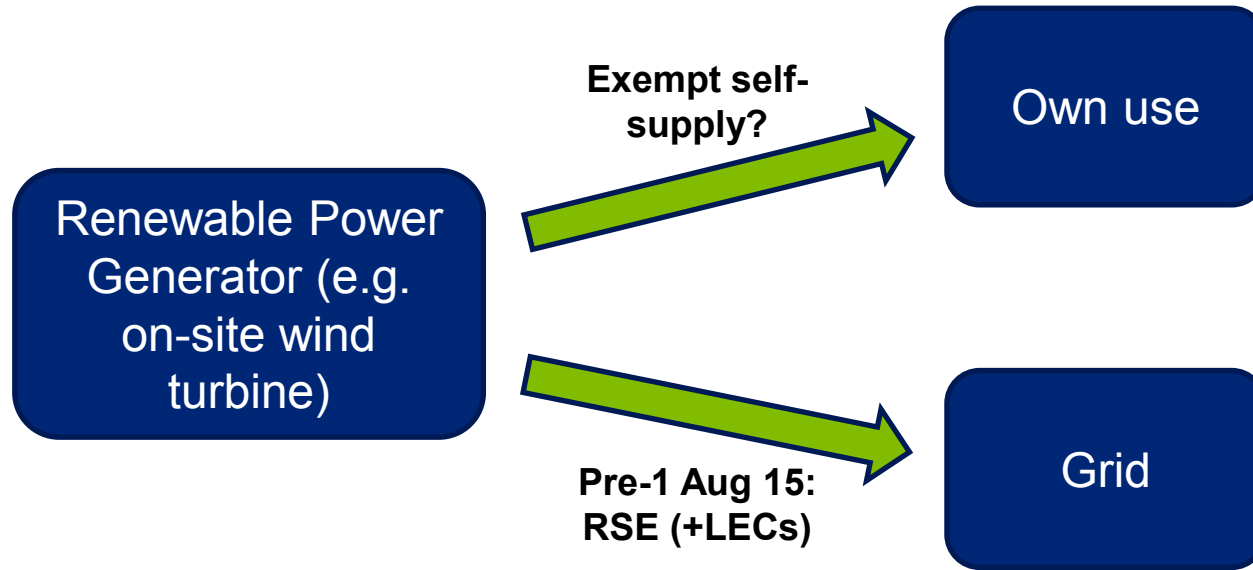
# Climate Change Levy: removal of the renewable source exemption

- The government announced in the Budget (July 2015) that the exemption from Climate Change Levy (CCL) for renewable source electricity (RSE) would be removed from 1 August 2015.
- Rationale:
  - any added value of the RSE will be negligible by the early 2020s due to other means of support on offer to renewable generators.
  - concern that the financial benefit of the RSE has increasingly been available to offshore generators.

# Removal of the RSE: implications for businesses

- LECs will not be issued for any power generated from 1 August 2015, and the power will not be eligible for CCL exemption
- A transitional period will apply providing an opportunity for businesses to use up any LECs that they held at 1 August 2015
- Impact on the value of LECs currently held?
- Affected businesses should review their contractual arrangements
- System changes will need to be considered in terms of invoicing, credits and rebills from 1 August
- Investors: consider impact on costs/prices
- Judicial review proceedings?

# Implications for businesses: on site generation



- Self-supply exemption for auto-generators or exempt unlicensed electricity suppliers – for CHP, stand-by generators or small generating stations
- Removal of RSE: stronger incentive to use electricity on site (or supply off-Grid) due to the lower CCL cost
- Directed utilities: ‘self-supply’ exemption does not apply

# Climate Change Agreements (CCAs)

## Environment Agency: progress report 2013 and 2014

Details the energy efficiency and emission reductions achieved in the period between 1 January 2013 – 31 December 2014.

- 40 sectors achieved targets, 11 failed to meet targets and 2 did not operate in the period.
- 51% of target units either met or over-performed against targets.
- 49% of target units under-performed against targets:
  - Many of these chose to pay the 'buy-out' fee of £12/tonne of CO<sub>2</sub>e to remain eligible to receive the CCL discount;
- Net-over performance in target period – 2.1 million tonnes of CO<sub>2</sub>e (i.e. fewer emissions as a result of the CCA).
- To what extent can the reduction in emissions be attributed to CCAs?
- Likely to inform wider policy discussions on incentives/reform of the tax landscape

# CCAs – potential changes

How effective is the CCA as a policy measure?

- Dual purpose – protection and energy efficiency.
- Does it force the right type of behaviour, e.g. is the ‘buy-out’ price for underperformance too low?
- Cost-effective for government but is it the same for business?

Current state of play

- Change over time to the sectors classed as energy intensive?
- Introduction of new sectors potentially dilutes the measure?
- Introduction of the data centre sector in July 2015 – evidence of improvement in energy stewardship in the sector.

Looking ahead

- Is it the right mechanism to protect certain industry sectors?
- Potential extension?
- Is there enough of an incentive given the removal of the CCL exemption for RSE?
- Ongoing dialogue and debate as part of the simplification of the UK policy environment

# Landfill Tax

## Devolution of Landfill Tax (LFT):

- **Scotland:** LFT devolved to Scotland from 1 April 2015 – standard rate of £82.60 per tonne and lower rate of £2.60 per tonne
- **Wales:** From April 2018, Wales will have control over setting and collecting its own landfill tax.

## Waste Recycling Group (WRG) – judicial review:

- Application for judicial review by a number of landfill operators who were refused repayments of Landfill Tax after HMRC changed its view on the application of the decision in WRG
- HMRC appealed against the application for judicial review
- July 2015: Court of Appeal dismissed HMRC's appeal. Judicial review is set to proceed

# Aggregates Levy

## State Aid

- The European Commission opened a formal investigation into certain UK aggregates levy (AL) exclusions, exemptions and reliefs in 2013
- As a result, the Government suspended certain exemptions with effect from 1 April 2014.
- The European Commission announced in March 2015 that the exemptions are lawful – except for shale aggregate removed in specific circumstances
- Budget 2015 announced that the exemptions would be reinstated from 1 August 2015
- Businesses can make claims for over-paid AL for the period in which the exemptions were suspended

# Aggregates Levy

## Northumbrian Water Ltd (NWL) – Upper Tribunal decision

- Aggregate was extracted from a pit and used to construct dams and a causeway at a reservoir 500m away.
- Key question: were the pit, the dam and the reservoir part of the same site?
- The First-tier Tribunal (FTT) ruled that the “site” included both the pit and the locations where gravel was used. It rejected HMRC’s narrow definition of a “site”. HMRC appealed.
- The Upper Tribunal found that there was no error of law by the FTT and confirmed the position that the aggregate was not subject to AL.
- Businesses should take care surrounding the application of AL where aggregate is moved across a large site.



# Europe

# EC report: Tax Reforms in EU Member States

- The annual report on Tax Reforms in EU Member States addresses tax policy challenges for economic growth and fiscal sustainability.
- Environmental taxes ‘doubly attractive’:
  - Growth-friendly
  - Help Member States achieve environmental policy objectives
- Environmental taxes: one of several policy instruments used to reduce pollution.
- Taxes on energy generate the most revenue out of environmentally-related taxes.
- Low energy prices: an opportunity to reform energy taxation?

# EC report: general trends across Member States

A mixed picture!

- Increased rates on excise duties on energy in around a third of Member States... but reductions in 5 countries
- Introduction or reinforcement of tax incentives to promote the use of renewable energy sources and encourage energy efficiency... others phasing out.

Broad policy direction appears to be towards increased rates of environmental taxes, and implementation/reform of policies to meet the UN 2030 climate and energy goals.

# French carbon tax

- The French government passed an energy bill in July which aims to reduce the country's fossil fuel consumption by 30% by 2030 and the level of greenhouse gas emissions.
- The rate of tax is set to increase to €56 per tonne of carbon dioxide in 2020 and to €100 in 2030.
- This marks a considerable increase from the rate of €7 per tonne of CO<sub>2</sub> on the consumption of natural gas, heating oil and coal when the domestic carbon tax was introduced last year.
- Businesses face an increase in tax liabilities due to this change and are encouraged to make appropriate changes, such as shifting to renewable energy, in order to mitigate the impact of this reform.

# Energy tax design across Member States

The Energy Tax Directive means there are some similarities in the way that energy products are taxed across Member States and the types of use/processes that qualify for relief.

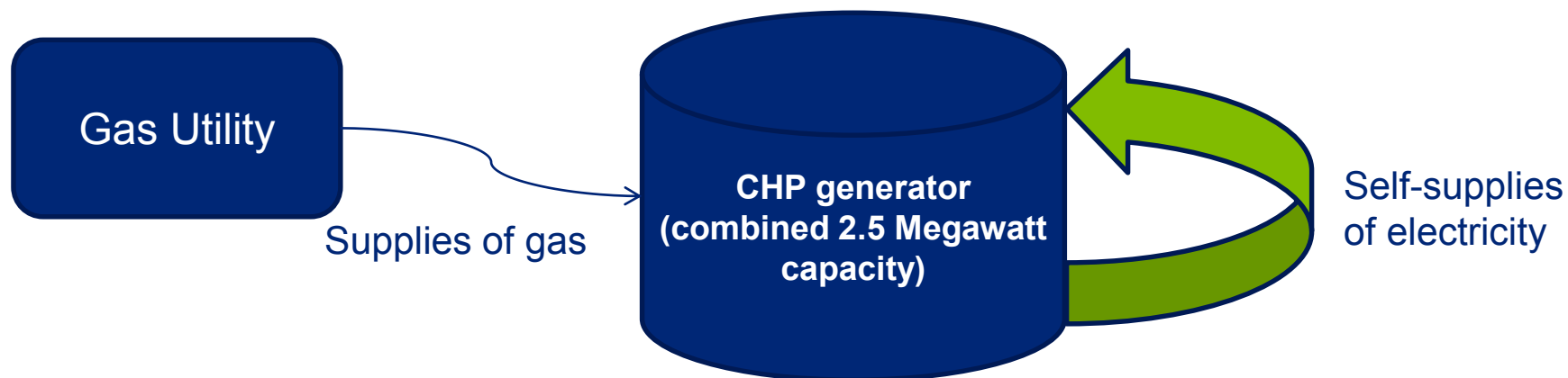
Some exemptions apply 'up front', but in other cases refunds have to be claimed after the tax has been paid.

- UK: climate change levy
  - Up front exemption from CCL subject to provision of relevant certificate
- Germany: power tax
  - A full refund of power tax is applicable for power consumed for industrial processes
  - A partial refund of €5.13 /MWh is applicable for the consumption of power by businesses in general

Businesses operating in other countries should be aware of the mechanics of energy tax reliefs (and ensure they take advantage of available reliefs)

# Case studies

## Case Study 1 – On site generation



### Background:

- Gas-fired CHP generator
- All electricity produced is self-consumed - no supplies made to either the Grid or to another customer.
- Not a standby generator.
- No CCL registration in place for the generator and CCL charged at the main rates by gas utility.

### Discussion points:

1. Is a CCL registration required under the provision of the CPF legislation?
2. Should the gas utility charge CCL at the main rates? What are the requirements to demonstrate exemption?

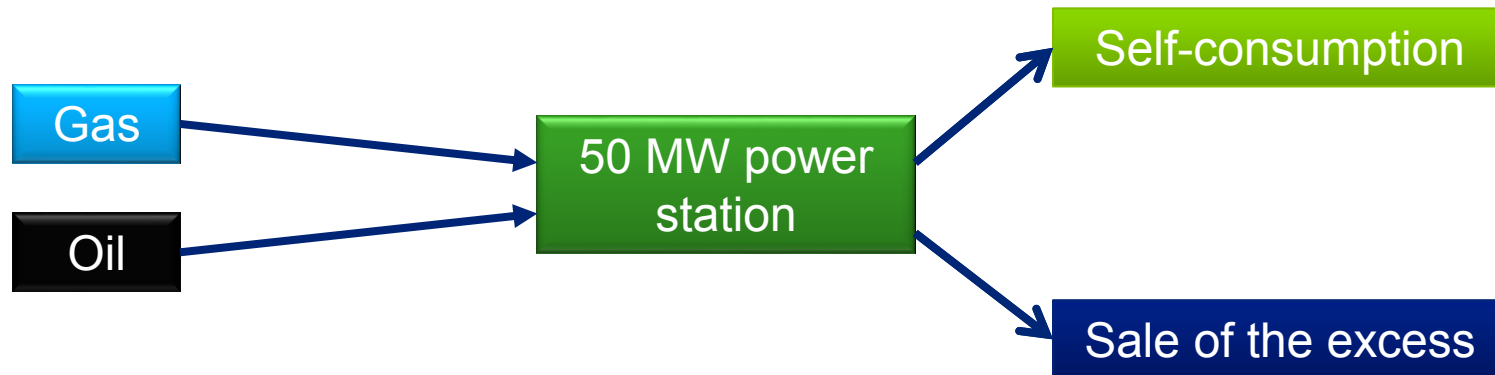
## Case Study 1 - On site generation

- The generator will be treated as an ordinary generator for CCL purposes, i.e. not “good quality” under the CHPQA scheme. CCL exemptions not available.
- Excess of 2MW generating capacity - unlikely to be considered “small”.
- From 1 April 2013, generators required to self-account for the carbon price support rates of CCL on the gas supplied for electricity generation.
- CCL registration triggered by these provisions.
- CCL at the main rates not due. PP11 should have been completed and submitted to the gas utility to ensure that CCL is not applied at the main rates on gas supplies. This should avoid “double-taxation” on the same supply of gas.
- Many businesses caught unaware by the new CPF legislation/rules - particularly those not in the business of electricity generation. The legislation can be difficult to navigate and it is easy to misinterpret the provisions.
- Prudent to check position as amounts could be material. Prompted disclosures should mitigate the severity of penalties.



# Case Study 2 – On site generation

## Gas & Power Station



### Background:

- CCL at the main rates is charged on the inputs
- Excise duty is charged on the oil inputs

### Discussion points:

1. Should CCL be chargeable on outputs?
2. CPS rates of CCL on inputs?
3. Does the business operating the power station have the ability to claim a refund for CCL and duty on inputs?

## Case Study 2 – On site generation

- Fossil fuels used to generate electricity – main rates of CCL applied by gas supplier and oil charged with excise duty.
- Generator required to account for CPS rates of CCL on the gas inputs.
- PP11 certificates should be completed and provided to gas supplier so as to ensure that the main rates of CCL are not applied on supplies of gas.
- CCL on self-supplies – main rates of CCL are in principle due on self-consumption of electricity.
- CCL on self-supplies of electricity: will any exemptions apply?
- Excise duty charged on oil inputs for electricity generation.
- Possible that generator can claim relief for excise duty if it isn't considered an auto-generator for CCL purposes.

# Case Study 3 – Errors and Penalties

## **Current HMRC focus on on-site usage / self-supplies**

- Gives rise to a CCL registration
- Failure to notify HMRC – what are the implications for assessments?
- Penalties – and which regime?
- Penalty interest
- When is there a ‘reasonable excuse’?



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