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DIRECTORATE-GENERAL
TAXATION AND CUSTOMS UNION
Indirect Taxation and Tax administration
Value added tax

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VALUE ADDED TAX COMMITTEE
(ARTICLE 398 OF DIRECTIVE 2006/112/EC)
WORKING PAPER NO 1017

CONSULTATION
PROVIDED FOR UNDER DIRECTIVE 2006/112/EC

ORIGIN:	**Spain**
REFERENCE:	**Article 102**
SUBJECT:	**Application of a reduced VAT rate to certain supplies of electricity**

1. INTRODUCTION

Article 102 of the VAT Directive[1] provides that Member States may apply a reduced VAT rate to the supply of natural gas, electricity or district heating after consulting the VAT Committee.

In accordance with Article 102, Spain has submitted a consultation to the VAT Committee in view of applying a reduced VAT rate of 10% to certain supplies of electricity. Currently, supplies of electricity are taxed in Spain at a standard rate of 21%.

The measure is temporary and would apply until 31 December 2021.

Spain points to the social dimension of the measure in question as it would affect mainly consumers in a situation of risk of social exclusion. However, any household and any consumer could potentially benefit from it. Moreover, the measure favours the process of electrification of the economy as the most efficient and effective means for reducing the emissions connected to the energy uses. It is linked to the implementation of the Spanish National Integrated Plan for Energy and Climate 2021-2030. It is noted that such a measure would be in line with the policy objective of the current Commission to make Europe carbon-neutral by 2050.

The text of the consultation is annexed to this document.

2. SUBJECT MATTER

The measure at issue has an exceptional and provisional character, and would apply until 31 December 2021.

Spain plans to apply a reduced rate of 10% to the supply, importation and intra-Community acquisition of electric energy, where the acquirer is:

a) an electricity supply contract holder where the contracted power (referred to the fixed component of power) is not higher than 10 KW, independently of the voltage level of the supply and the modality of contract, and when the arithmetic average price in the daily market corresponding to the last month prior to the last day of the invoicing period has exceeded the amount of 45 euros/MW,

b) an electricity supply contract holder who is beneficiary of the so-called "electricity social vouchers" and has been recognised as "severely vulnerable" or "severely vulnerable in risk of social exclusion" in conformity with Royal Decree 897/2017, of 6 October 2017, on the concept of vulnerable consumer, the social voucher and other protective measures for the domestic consumers of electric energy.

In further exchanges with the Commission services, Spain clarified that the reduced rate would apply to the price paid for the supply of electricity as a whole, including both fixed and variable components (depending on the real consumption) related to the supply (grid tariffs, charges, energy and other taxes). The fixed component in the Spanish proposal is

[1] Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ L 347, 11.12.2006, p. 1).

only relevant to determine whether one of the conditions for the application of the reduced VAT rate is met: when the contracting power is no higher than 10 KW (referring only to the fixed component of the contract).

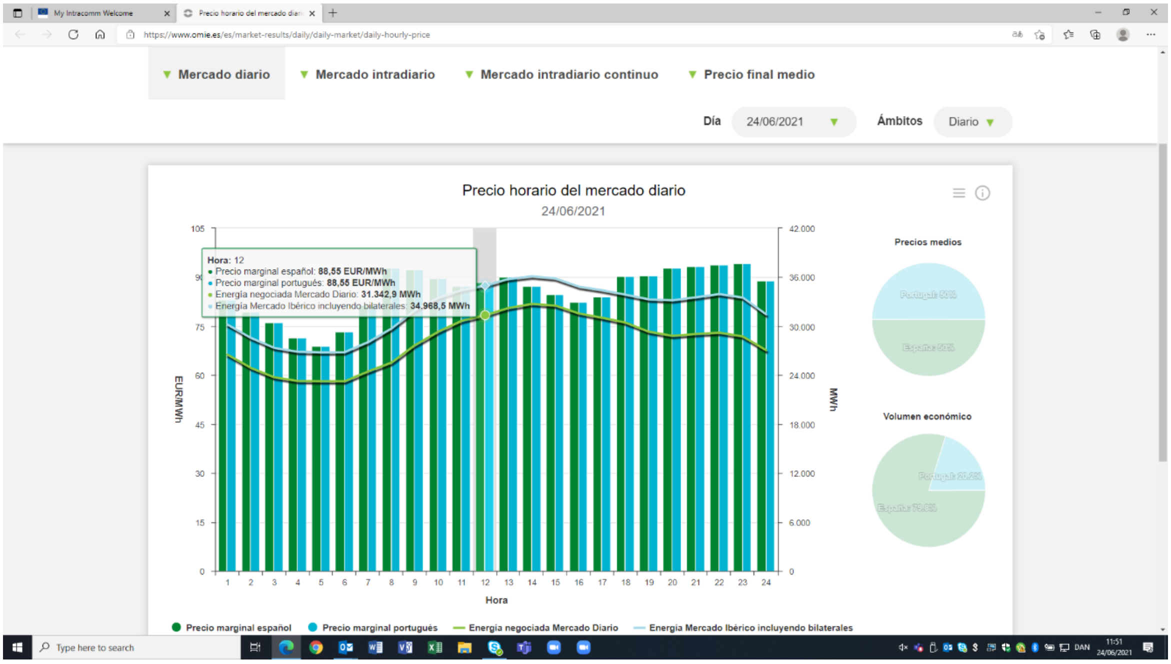
As regards the calculation of the arithmetic average price in the daily market corresponding to the last month prior to the last day of the invoicing period, Spain has provided the following explanation.

OMIE (acronym meaning "Operador de Mercado Ibérico de la Electricidad") is the electricity market operator for the Iberian area. In terms of Regulation (EU) 2019/943 of the European Parliament and the Council, of 5 June 2019, on the internal market for electricity, OMIE is Spain's "NEMO", that is, the market operator designated by the competent authority to carry out tasks related to single day-ahead or single intraday coupling. OMIE publishes on a daily basis the day-ahead price for both Spain and Portugal for every hour of the following day:
https://www.omie.es/es/market-results/daily/daily-market/daily-hourly-price

The arithmetic average price in the daily market corresponding to the last month prior to the last day of the invoicing period is determined by taking the published price for every day set by the OMIE and calculating the arithmetic average for the whole month (that price is determined for the wholesale market).

In order to check whether this price is above or below the 45 euros/MWh threshold, the suppliers can calculate the average of this price for the previous calendar month based on public and transparent information or can simply take this value from the OMIE website. One can consult the evolution of the monthly average price - based on the daily arithmetic average price - of electricity under the following link:
https://www.omie.es/es/market-results/annual/daily-market/daily-prices?scope=annual&year=2021

As an example, if an electricity bill is issued on 25 June, covering the electricity consumption for the period between 25 May and 24 June, the relevant monthly average price (again based on arithmetic average of published daily price) will be the price for May, since this is the last complete calendar month prior to the final date of the bill. In this example, that would amount to 67.12 euros/MWh; see the graph below:



In a further exchange following the submission, Spain indicated that 94.24% of the electricity contracts would benefit from the measure. The beneficiaries of the measure would be composed in 97.5% of domestic consumers and in 2.5% of businesses. Moreover, as regards the impact of the measure on VAT revenue, Spain clarified that according to its best assessment, it would be EUR 566 million (in the submission, this figure was rounded up to EUR 600 million), which would represent 0.78% of annual VAT revenue. This figure refers to an annual calculation if the measure had an impact from 1 January 2021.

The judgment of the Court of Justice of the European Union (CJEU) in Case C-384/01 is mentioned[2], in which the CJEU found that application of reduced rates to certain supplies was consistent with the principle that exemptions or derogations must be interpreted narrowly.

The Spanish authorities argue that, since electricity supplies are taxed at the place where the customer effectively uses and consumes them, no distortion of competition between Member States may arise. Likewise, despite the fact that the measure is partly targeted at consumers at a risk of social exclusion, any consumer fulfilling the conditions set by Spain can benefit from it and as a result no distortion of competition among taxpayers would be possible.

3. THE COMMISSION SERVICES' OPINION

The Commission services take note of the intention of Spain to apply a reduced VAT rate of 10% to certain supplies of electricity, notably to the supply, importation and intra-Community acquisition of electric energy, where the acquirer is:

2 Judgment of 8 May 2003, case C-384/01, *Commission v France*, EU:C:2003:264.

a) an electricity supply contract holder where the contracted power (referred to the fixed component of power) is not higher than 10 KW, independently of the voltage level of the supply and the modality of contract, and when the arithmetic average price in the daily market corresponding to the last month prior to the last day of the invoicing period has exceeded the amount of 45 euros/MW,

b) an electricity supply contract holder who is beneficiary of the so-called "electricity social vouchers" and has been recognised as "severely vulnerable" or "severely vulnerable in risk of social exclusion" in conformity with Royal Decree 897/2017, of 6 October 2017, on the concept of vulnerable consumer, the social voucher and other protective measures for the domestic consumers of electric energy.

Spain would apply the measure under the present consultation as soon as the consultation procedure with the VAT Committee is completed.

In light of the information available, the Commission services underline the following:

It is noted that despite the fact that the measure is partly targeted at consumers at a risk of social exclusion, in principle any consumer fulfilling the conditions set by Spain can benefit from it. Although the reduced rate will certainly favour electricity supply contract holders who are beneficiaries of "electricity social vouchers" and have been recognised as "severely vulnerable" or "severely vulnerable in risk of social exclusion", it will also apply to consumers who are not at risk of social exclusion. In particular, it will apply to households (mostly) whose contracted power is not higher than 10 KW, when the arithmetic average price in the daily market corresponding to the month prior to the last day of the invoicing period has exceeded the amount of 45 euros/MW.

The Commission is determined to tackle the challenges of climate change and environmental degradation. Both the Commission President von der Leyen and the Commissioner for Economy Gentiloni have consistently declared their commitment to promote and implement ambitious environment, climate and energy policies. This commitment is illustrated in the Commission communication on 'The European Green Deal'[3], presented on 11 December 2019, which refers to specific actions in this regard that constitute clear political priorities for the Commission. Spain expects the measure to contribute to the reduction of emissions linked to energy uses and thus have a positive impact on the protection of the environment. Such a measure aiming at reducing the negative impact on the environment would be in line with the objectives of the European Green Deal.

Spain refers to the judgment of the CJEU in Case C-384/01[4], in which the CJEU ruled that the fiscal neutrality principle, which precludes treating similar goods, which are thus in competition with each other, differently for VAT purposes was not infringed by the selective application of the reduced VAT rate to certain supplies of electricity, provided that no risk of distortion of competition existed. Since the reduced VAT rate is the exception to the general rule that the standard VAT rate is applicable, the restriction of its application is in line with the principle according to which exemptions or exceptions have to be interpreted restrictively.

[3] Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions 'The European Green Deal', COM(2019) 640 final.

[4] See footnote 2.

In this light, the selective application of a reduced VAT rate to certain supplies of electricity, as proposed by Spain, could be seen as consistent with the principle of fiscal neutrality on condition that it may not lead to a distortion of competition. In this regard, Spain states that the measure contemplated does not lead to distortions of competition, as limit in the contracted power of 10 KW will allow the measure to benefit practically every household as a final consumer. The measure is open in principle to any consumer fulfilling the conditions set. Moreover, Spain submits that that the natural gas network does not reach many points of the Spanish territory and, hence, the alternative to electricity in those areas are the derivatives of petroleum, which cannot be subject to a reduced rate under the VAT Directive. The Commission services note that the determination of whether the intended measure is likely to cause competition concerns in the domestic market should be left first and foremost to the competent national authorities.

Spain also submits that the measure would not result in a distortion of competition between Member States. In this regard, it is pointed out that, according to Council Directive 2009/162/EC[5], the rules for determining the place of taxation of electricity determine that VAT is levied at the place where electricity is actually consumed. They thus ensure that the likelihood of distortion of competition between Member States is minimal.

Based on the information provided by the Spanish authorities, the intended measure appears likely to contribute to the objectives of the European Green Deal, provided that it does not lead to a compromise of the principle of fiscal neutrality or a distortion of competition in the Single Market and given its limited impact on the national VAT revenue.

The Commission services have no further comments in addition to the ones made above.

3. DELEGATIONS' OPINION

Delegations, in particular Spain, are invited to express their views on the matters raised and the observations made by the Commission services.

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[5] Council Directive 2009/162/EU of 22 December 2009 amending various provisions of Directive 2006/112/EC on the common system of value added tax (OJ L 10, 15.1.2010, p. 14).

ANNEX

Consultation of the Kingdom of Spain to the VAT Committee in respect of the option on Article 102 of Directive 2006/112/EC. Enquiry for launch of written procedure

As foreseen in article 102 of the Directive 2006/112/EC of the Council, of 28 November 2006, on the common system of value added tax (hereinafter, VAT Directive) the Kingdom of Spain plans to introduce in its national VAT legislation a 10% reduced rate applicable to certain supplies of electricity.

The measure has to be adopted with an urgent character, so the launch of the written procedure for the consultation of the VAT Committee seems to be the most appropriate mechanism.

Legal Background

Article 98 of the VAT Directive establishes that Member States may apply either one or two reduced rates. Reduced rates can only be applicable to the supply of goods and services in the categories described in the Annex III of the Directive.

Nevertheless, Article 102 of the VAT Directive establishes that, after consultation of the VAT Committee, each Member State may apply a reduced rate to the supply of natural gas, electricity, or district heating.

Object of the Measure

The Kingdom of Spain has the intention to tax certain supplies of electricity with a 10 per cent reduced rate. Currently, supply of electricity and natural gas are taxed at our general tax rate of 21 per cent.

The measure implies with an exceptional and provisional character, and until 31 December 2021, the application of a reduce rate of 10 per cent to the supply, importation and intracommunity acquisition of electric energy, where the acquirer is any of the following:

a) a electricity supply contract holder where the contracted power (referred to the fixed component of power) is not higher than 10 KW, independently of the voltage level of the supply and the modality of contract, and when the arithmetic average price in the daily market corresponding to the last month prior to the last day of the invoicing period has exceeded the amount of 45 euros/MW.

b) a electricity supply contract holder who is beneficiary of the so-called “electricity social vouchers” and have been recognised as “severe vulnerable” or “severe vulnerable in risk of social exclusion” in conformity with Royal Decree 897/2017, of 6 of October, on the concept of vulnerable consumer, the social voucher and other protection measures for the domestic consumers of electric energy.

The European Court of Justice, on its sentence of 8 of May 2003, C-384/01, stated that the introduction and application of VAT reduced rates lower than the general rate can be admitted if it does not vulnerate the principle of neutral fiscality inherent to the VAT common system and which opposes that similar goods, in competence among them, are treated differently from the VAT point of view.

Considering that the supply of electricity is currently taxed in the place where the consumer effectively uses and consumes the electricity, there is no distortion of competition among Member States. On the other hand, even when some of the situation activating the measure will affect only consumers in situation of risk of social exclusion, any consumer can potentially benefit from the reduction of the rates in the case described in the above-mentioned letter a), whenever the conditions for its application concur, so no distortion of competition is to be found among consumers neither.

Furthermore, even when the reduction of the VAT rates for the natural gas is not at stake, we have to bear in mind that the natural gas network does not reach many points of the Spanish geography where the alternatives to electricity are the derivate products of petrol, which are never covered by Article 102 of the VAT Directive.

Additionally, the European Court of Justice in the case C-384/01 understood that a selective application of a reduced rate to certain supplies is coherent with the principle according to which exemptions or exceptions have to be interpreted restrictively.

It should be noted that the general measure is conditional upon a situation where the average monthly price of the wholesale market, during the month prior to the month of invoicing, has exceeded 45 euros/MW, always when the contracted power (the fixed component of power) is not higher than 10 KW, so consequently its application is conditioned and subordinated to such circumstances being, in any case, a temporary measure for the remainder of year 2021.

To this end, it has to be taken into account that the threshold of 45 euros/MW is connected with the average exchange price during December 2020 for the electricity delayed-delivery contracts in Spain for 2021 (period of the application of the measure).

On the other hand, the establishment of a limit in the contracted power of 10 KW will allow the measure benefiting practically every household final consumer.

Finally, the measure directly favour the implementation of the National Integrated Plan for Energy and Climate 2021-2030 (PNIEC, in its Spanish acronyms), which contemplates the commitment and contribution of the Kingdom of Spain to the international and European efforts for the adoption of measures for the decarbonisation of the energetic system and the encouraging and expansion of the renewables energies, since the measure favours the process of electrification of the economy as a the most efficient and effective mean for reducing the emissions connected to the energetic uses.

Period of application

The measure will be applicable from the entry into force of the legal instrument and until the 31 December 2021.

Impact of the measure in the VAT public revenues

It is expected that the impact in the VAT collection during its application, in the case the circumstances for the activation of the measure concur, will amount to 600 million euros.