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**WORKING LANGUAGE**

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**Subject: State aid case NN 1/2005– Denmark  
'Water tax relief for VAT registered companies'**

Sir, Madam,

The Commission wishes to inform Denmark that, having examined the information supplied by your authorities on the aid referred to above, it has concluded that the full exemption of the tax on water in favour of VAT registered companies does not constitute State aid.

#### **1. PROCEDURE**

By letter dated 15 September 2004, registered at the Commission's Secretariat-General on 16 September 2004 (SG/2004/A/9924), the Danish authorities notified the Commission pursuant to Article 88(3) of the EC Treaty of the water tax relief for VAT registered companies. As the relief from the Danish act on water tax has been granted since 1 January 1994, the scheme has been handled as a non-notified case.

By letter dated 29 October 2004 (D/57733), the Commission asked for additional information, which was received by letter dated 23 December 2004, registered at the Commission on 3 January 2005 (SG/2005/A/4).

Udenrigsminister  
Per STIG MØLLER  
Asiatisk Plads 2  
DK - 1448 KØBENHAVN K

## 2. DESCRIPTION OF THE MEASURE

In Denmark, a tax of DKK 5 per m<sup>3</sup> water supplied through the pipe network<sup>1</sup> was introduced on 1 January 1994. The legal basis for the water tax is Act on tax on water supplied through the pipe network. In addition to the objectives of the tax to generate State revenue, the tax has, according to the Danish authorities, the following positive environmental effects:

1. *It steers to an efficient maintenance of the water distribution system in order to minimise the water leakage.* According to preparatory law work<sup>2</sup> the costs of a water plant (administrative costs as well as the costs of establishment of the distribution net, etc) are in the short term in principle independent of the water consumption. If business consumption would not be exempted, the tax system would, thus, favour consumers with low water consumption.
2. *It leads to lower water consumption which results in less waste water.* As waste water has to be cleaned to fulfil the requirements for water discharge which are set out in the Danish environmental water plan, the amount of contamination is directly proportional to the water consumption of households. This proportionality is not applicable to business consumption. In order to reduce the content of the discharge of waste water, there is a special tax for such discharge. That tax is paid by households as well as businesses.
3. *It leads to a decreased use of ground water.* According to the preparatory law work<sup>3</sup>, there is no lack of ground water of good quality in Denmark. Decreasing the use of ground water is though not the objective of the tax, but rather an environmental positive effect that is the consequence of the tax.

Due to the reasons set out in point 1-3 with respect to business consumption, the general rationale of the water tax system is to only tax household consumption of water.. In order to distinguish between household consumption and business consumption, the Danish legislation uses the VAT criterion. Companies that are not registered for VAT are considered to have water consumption comparable to that of households. Consequently, all VAT registered companies are exempted from the tax, while households and non-VAT registered companies pay the tax in full. Businesses which are not obliged to register for VAT can choose to register voluntarily, which according to the Danish authorities many small businesses do.

The tax is paid by the water suppliers, who are obliged to hold a register over the clients to whom they have supplied water. The suppliers transfer the cost to the consumer by including it in the water price. The rebate is provided to VAT registered companies on a quarterly basis through a deduction of the tax in the VAT declaration.

The duration of the relief for business consumption from the water tax is not limited.

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<sup>1</sup> Water in bottles, paper, etc, which is sold in the retail trade is not subject for tax.

<sup>2</sup> See p. 7 of the Explanatory memorandum to the Act no. 639 of 21 August 1998 on tax on water distributed through the pipeline.

<sup>3</sup> See p. 6 of the Explanatory memorandum to the Act no. 639 of 21 August 1998 on tax on water distributed through the pipeline.

All VAT registered companies are covered by the relief. The number of VAT registered companies in Denmark is ca 400 000. According to the Danish authorities, there are presently ca 15 000 businesses which are not VAT-registered.

On the basis of budget amounts from previous years, the refund of the water tax to VAT registered companies amounts to ca. DKK 560 million (ca. €75 million) per year.

### 3. ASSESSMENT

#### 3.1 Presence of State aid under Article 87(1) of the EC Treaty

The Commission has assessed the notified scheme on the basis of Article 87(1) of the EC Treaty. That Article states that any aid granted through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, insofar as it affects trade between Member States, be incompatible with the common market.

The scheme results in a loss of State revenue, i.e. it is financed from State resources.

In 1998, the Commission published a notice on the application of the State aid rules to measures relating to direct business taxation<sup>4</sup> ('the Commission notice'). According to point 13 of that notice, tax measures which are open to all economic agents operating within a Member State are in principle general measures. They must be effectively open to all firms on an equal access basis and they may not *de facto* be reduced in scope through, for example, the discretionary power of the State to grant them or through other factors that restrict their practical effect.

This has been confirmed in case-law of the Court of Justice. For example, in case C-143/99 "Adria-Wien Pipeline GmbH and Wietersdorfer & Peggauer Zementwerke GmbH v Finanzlandesdirektion für Kärnten" of 8 November 2001<sup>5</sup>, the Court stated that a measure that benefits all undertakings in national territory, regardless of their activity, does not constitute State aid.

If the tax authority has discretionary freedom to fix different tax treatment for different taxpayers, there is normally a presumption of aid<sup>6</sup>. In this case, the implementation of the measure is made by using the VAT criterion. Any business can register for VAT incurring only small compliance costs and all VAT-registered companies are exempted from the water tax. The tax authority does, thus, not have discretionary freedom to set different tax rates for different companies or groups of companies. The use of the VAT criterion is a practical solution to distinguish between household consumption and business consumption and to handle the refund in an administratively efficient and objective way. It does not favour certain sectors or regions. There is, thus, no indication that the practical use of the VAT declaration leads to that certain undertakings are favoured compared to others and that the scheme would be selective.

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<sup>4</sup> Commission notice on the application of the State aid rules to measures relating to direct business taxation (hereafter referred to as 'the Commission notice'), OJ C 384, 10.12.1998, p. 3

<sup>5</sup> See for example C-143/99 Adria-Wien Pipeline GmbH and Wietersdorfer & Peggauer Zementwerke GmbH v Finanzlandesdirektion für Kärnten, [2001] ECR I-8365, paragraph 35-36.

<sup>6</sup> See point 21 and 22 of the Commission notice.

On the basis of the above, the Commission finds that the scheme is a general measure, i.e. it is not selective. The refund does therefore not constitute State aid in the meaning of Article 87(1) of the EC Treaty.

#### 4. CONCLUSION

The Commission has accordingly decided that NN 1/2005 'Water tax relief for VAT-registered companies' is a general measure. It does, thus, not constitute State aid within the Article 87(1) of the EC Treaty and Article 61(1) of the EEA Agreement.

The Commission reminds the Danish authorities that, in accordance with Article 88 (3) of the EC Treaty, plans to modify this scheme so that it becomes State aid have to be notified to the Commission pursuant to provisions of Commission Regulation (EC) No 794/2004 implementing Council Regulation (EC) No 659/1999 laying down detailed rules for the application of Article 93 [now 88] of the EC Treaty (OJ L 140, 30.4. 2004, p.1).

This decision is without prejudice to the compatibility with Directive 2000/60/EC of the European Parliament and of the Council of 23 October 2000 establishing a framework for the Community action in the field of water policy<sup>7</sup>. Article 9 of that directive states that Member States shall ensure by 2010 that water-pricing policies provide adequate incentives for users to use water resources efficiently. Therefore, the Danish authorities may have to review their national legislation by that date to take into account the stipulations of that directive.

If this letter contains confidential information, which should not be disclosed to third parties, please inform the Commission within 15 working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site:

[http://europa.eu.int/comm/secretariat\\_general/sgb/state\\_aids/](http://europa.eu.int/comm/secretariat_general/sgb/state_aids/).

Your request should be sent by registered letter or fax to:

European Commission  
Directorate-General for Competition  
State Aid Registry  
B-1049 Brussels  
Fax No: +32-2-296 12 42

Yours faithfully,  
For the Commission

Neelie KROES  
Member of the Commission

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<sup>7</sup> OJ L 327, 22.12.2000, p. 1