



EUROPEAN COMMISSION

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In the published version of this decision, some information has been omitted, pursuant to articles 24 and 25 of Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty, concerning non-disclosure of information covered by professional secrecy. The omissions are shown thus [...].

**PUBLIC VERSION**

**WORKING LANGUAGE**

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**Subject: N 44/2005 – Lithuania**  
**Excise tax reduction on biofuels**

Excellency,

## **I. PROCEDURE**

- (1) By letter dated 14 January 2005, registered on 19 January 2005, Lithuania notified its intention to introduce an excise duty reduction in favour of certain biofuels. The Commission requested further information by letters of 24 February 2005 and 2 May 2005, to which Lithuania replied by letter dated 5 April 2005, registered on 7 April 2005 and by letter dated 31 May 2005, registered on 6 June 2005.

## **II. DESCRIPTION**

- (2) The notified aid scheme consists of a reduction in the excise tax on biofuels blended with other fuel. The excise duty exemption for biofuels applies only to the biofuel component of the mixture. Consequently, the tax rate of excise duty to be applied to blended biofuel products will be reduced according to the proportion of biofuel in the final blend.

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- (3) The Lithuanian Republic wishes to promote the production and use of blended biofuels. The objective of the notified scheme is to assist Lithuania in meeting the targets set out in Directive 2003/30/EC of the European Parliament and of the Council of 8 May 2003 on the promotion of the use of biofuels or other renewable fuels for transport<sup>1</sup>. The scheme will favour the production and use of biofuels, contribute to the initial development of the market for biofuels in Lithuania and reduce the Lithuanian energy sector's dependence on petroleum-based fuels and motor fuels.
- (4) The state aid is notified under the Community guidelines on State aid for environmental protection<sup>2</sup>. The scheme will only enter into force after the Commission's approval<sup>3</sup> and the duration will be limited to an initial period of five years, i.e. from the date of the Commission's decision until 31.12.2010.
- (5) Under the notified aid scheme, Lithuania intends to introduce a reduced excise duty tax rate for the following categories of biofuels for transport:
- (a) bioethanol – ethanol produced from biomass<sup>4</sup> (e.g. grain) and/or the biodegradable fraction of waste, to be used as biofuel. It would substitute petrol;
  - (b) biodiesel – a methyl (ethyl)-ester produced from vegetable or animal oil, of diesel quality, to be used as biofuel. It would substitute diesel;
  - (c) bio-ethyl-tertio-butyl-ether – ETBE produced on the basis of bioethanol. The percentage by volume of bio-ETBE that is calculated as biofuel is 47%;
  - (d) pure vegetable oil – oil produced from oil plants through pressing, extraction or comparable procedures, crude or refined but chemically unmodified, when compatible with the type of engines involved and the corresponding emission requirements. It complies with the standard LST EN 14214.
- (6) The biofuel would be blended with the fossil fuel. Subsequently, the reduction in the amount of the duty paid under the proposed scheme will be proportionate to the volume of the biofuel in the end product. The products concerned are:
- ▶ blended diesel – biodiesel with 3-5% volume content of rape methyl ester (RME) in the final blend. The excise tax will be reduced accordingly by 3-5%.
  - ▶ blended petrol - fuel petrol unleaded 95 octane blended with ETBE. The volume of ETBE in the blend has to be more than 7% but will not exceed 15%, which means that the volume content of ethanol in the final biofuel blend equates to a margin of 3.29-7.05%<sup>5</sup>. The excise tax will be reduced accordingly by 3.29-7.05%.

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<sup>1</sup> OJ L 123 of 17.5.2003, p. 42

<sup>2</sup> 2001/C 37/03

<sup>3</sup> It relates to the provisions laid down in the Republic of Lithuania Law on Biofuel, Bio Motor Fuels and Bio-Oils of 5 February 2004, where the Lithuanian Government has to ensure that by 31 December 2005 the proportion of biofuels for transport shall amount to at least 2 %, calculated on the basis of energy content, of all petrol and diesel for transport purposes placed on the national markets, and by 31 December 2010 – at least 5.75 %.

<sup>4</sup> Acc. to article 3 of the Republic of Lithuania Law on Biofuel, Biofuels for transport and Bio-Oils of 5 February 2004, "biomass" means products and waste from agriculture (including vegetal and animal substances), forestry and related industries or the biodegradable fraction of such products and waste, as well as the biodegradable fraction and municipal waste.

<sup>5</sup> The calculation relates to the volume of bio-ETBE as biofuel which is 47%.

- (7) Lithuania intends to introduce the excise duty exemption on the basis of the directive 2003/96/EC on energy taxation<sup>6</sup>. The national legal basis of the aid is provided by Article 38(4) of the recast version of the Excise Act of the Republic of Lithuania of 29 January 2004 and by the Republic of Lithuania Law on Biofuel, Bio Motor Fuels and Bio-Oils Act of 5 February 2004<sup>7</sup>.
- (8) Without exemption, an excise duty would be applied to bioethanol and biodiesel to the same extent as for petrol and diesel. Subsequently, the duty foregone as a result of the duty reduction for biofuels is expected to be approx. LTL 250 million (EUR 72.4 million)<sup>8</sup> over the period of five years. The amount is specified in the table 1:

**Table 1:** Estimated excise duty for fossil fuels, consumption of biofuels and duty foregone due to the excise tax reduction on biofuels in Lithuania in the period 2006-2010:

	2006	2007	2008	2009	2010	Total
<b>Excise duty for fossil fuels</b>						
Petrol (EUR per 1 ton)	382	382	430	430	430	2054
Diesel (EUR per 1 ton)	290	290	326	326	326	1558
<b>Consumption of biofuels</b>						
Bioethanol (in thousand ton)	12	12	15	17	20	76
Biodiesel (in thousand ton)	15	15	20	30	40	120
<b>Duty foregone or state aid amount</b>						
Bioethanol and biodiesel (in million EUR)	8.9	8.9	13.9	17.5	23.2	72.4

- (9) Lithuania will grant the excise relief by way of excise remission under the procedure established by the central tax administrator in Lithuania<sup>9</sup>. The duty reduction will be granted, provided that the biofuels concerned meet the specified definition, to any producers of biofuels in Lithuania as well as to any importer of biofuels from another Member State or third countries to Lithuania.
- (10) According to the Lithuanian national authorities, there is currently no regular market for biofuels in Lithuania. There are only a few enterprises that have launched experimental production of biofuels.

<sup>6</sup> Directive 2003/96/EC of the Council of 27.10.2003 restructuring the Community framework for the taxation of energy products and electricity, OJ L 283 of 31.10.2003, p. 51.

<sup>7</sup> Law amending the law on biofuel of Lithuanian Republic of 18 July 2000.

<sup>8</sup> The exchange rate applied is the following: 1 EUR = 3.4528 LTL (Lithuanian currency).

<sup>9</sup> Order No. VA-75, 29.04.2004 of the Lithuanian State Tax Inspectorate under the Ministry of Finance of the Republic of Lithuania reissuing permission to produced energy products containing additives of biologic origin.

- (11) The reduced excise duty is applicable to biofuels from whichever geographical origin. There are no budgetary or quantity limits; there is no quota system.
- (12) Lithuania will annually review the production costs of biofuels eligible for the excise tax reduction as well as the price movement of biomass relative to fossil fuel prices. The aid granting institution will annually gather information from the producers of biodiesel and bioethanol. If necessary, the aid for biodiesel will be adjusted in order to avoid any overcompensation and to keep the price of biofuel at the same level of that of conventional energy. Lithuania committed itself to providing annual monitoring reports to the Commission containing all relevant information on the production costs of the biofuels and the market price of fuels to show that there is no overcompensation.

### **III. ASSESSMENT**

#### **3.1 Existence of aid within the meaning of Article 87(1) EC Treaty**

- (13) According to Article 87 of the EC Treaty, State aid involves (1) an aid, granted by a Member State or through State resources, (2) which distorts competition, (3) by favouring certain undertakings, (4) insofar as it affects trade between Member States.
- (14) The proposed measure constitutes State aid in the meaning of Article 87(1) of the EC Treaty. It is granted by the Lithuanian State and financed through State resources as the exemption reduces tax income that otherwise would have been available to the State. The measure distorts competition as it selectively favours a limited number of producers of fuels only when they produce environmentally friendly fuels. The beneficiaries of the tax reduction should not be considered to be the final consumers of the fuel, as they are likely to pay a price that will be broadly equal to (if not higher than) the prices of the fuels that directly compete with the alternative fuel, namely traditional fuels. In contrast, the measure favours the producers of the alternative fuels, because they will obtain a higher return for their products. Biofuels serve as substitutes for fossil fuels and all kinds of fuels are widely traded between Member States. Therefore the measure is likely to affect trade between Member States in this sector.
- (15) Lithuania has complied with its obligation to notify the aid in accordance with Article 88(3) of the Treaty.

#### **3.2 Community policy with respect to environmentally friendly fuels**

- (16) The promotion of biofuels and other renewable fuels to replace diesel or petrol for transport is a well established Community priority, as they are expected to contribute to objectives such as reduction of CO<sub>2</sub>-emissions and an environmentally friendly security of supply. Most concretely, Article 3 of Directive 2003/30/EC of the European Parliament and the Council of 8.5.2003 on the promotion of the use of biofuels or other renewable fuels for transport<sup>10</sup> establishes a reference value of 5.75% of all petrol and diesel for transport purposes placed on their markets by 31 December 2010. For Lithuania, this entails that biofuel consumption in the period 2006-2010 should reach 76 000 tons for bioethanol and 120 000 tons for biodiesel.
- (17) Directive 2003/30/EC defines 'biofuels' to mean liquid or gaseous fuel for transport produced from biomass, where 'biomass' is defined as the biodegradable fraction of products, waste and residues from agriculture (including vegetal and animal

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<sup>10</sup> OJ L 123 of 17.5.2003, p.42.

substances), forestry and related industries, as well as the biodegradable fraction of industrial and municipal waste. ‘Other renewable fuels’ means renewable fuels, other than biofuels, which originate from renewable energy sources as defined in Directive 2001/77/EC of the European Parliament and the Council of 27 September 2001 on the promotion of electricity produced from renewable energy sources in the internal market<sup>11</sup> and used for transport purposes. Article 2 (a) of this directive lists the following renewable energy sources: wind, solar, geothermal, wave, tidal, hydropower and biomass, landfill gas, sewage treatment plant gas and biogases.

- (18) The policy on biofuels fits in logically with the wider policy of promoting renewable energy sources in general<sup>12</sup>. These Community objectives and policies are also reflected in the Community policy on energy taxation in Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity<sup>13</sup>. Article 16(1) of this Directive allows Member States to apply an exemption or a reduced rate of taxation on biofuels<sup>14</sup>. Art. 15(1) sub (a) allows (partial) exemptions in the field of pilot projects for the technological development of more environmentally-friendly products or in relation to fuels from renewable resources.

### 3.3 Compatibility of the aid with the common market

- (19) Article 87(3)(c) of the EC Treaty foresees an exemption to the general rule of incompatibility as stated in paragraph 1 of this Article for aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest.
- (20) The scheme grants aid to fuels that are more environmentally friendly than conventional fuels. The Commission therefore assessed the notified measure in the light of the Community Guidelines on State aid for environmental protection<sup>15</sup> (hereafter “the guidelines”). It is not excluded that some biofuels will concern agricultural products that are included in Annex I of the Treaty. The aid for these products falls within the scope of the Community guidelines for State aid in the agriculture sector<sup>16</sup> and is excluded from the scope of the environmental aid guidelines in conformity with point 7 of these guidelines. Section 5.5.3 of the guidelines for State aid in the agriculture sector, stipulates that in duly justified cases, such as aids for the development of biofuels, the Commission may also approve operating aid in cases where these can clearly be shown to be necessary to offset the additional cost arising from the use of environmentally

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<sup>11</sup> OJ L 283 of 27.10.2001, p.33.

<sup>12</sup> See, e.g., the Commission’s White Paper of 1997 on Renewable Energy Sources COM (1997) 599 final of 26.11.1997, the Green paper on energy supply safety in the European Union COM (2000) 769 of 29.11.2000, the Commission’s communication on alternative fuels for road transport and on a set of measures to promote the use of biofuels COM(2001) 547 of 7.11.2001.

<sup>13</sup> OJ L283 of 31.10.2003, p.51.

<sup>14</sup> Defined as products that are made up of, or contain, one or more of the following products: 1) products falling within CN codes 1507 to 1518 (various animal and vegetable fats and oils), 2) products falling within CN codes 3824 90 55 and 3824 90 80 to 3824 90 99 (certain mixtures of esters and glycerol) for their components produced from biomass, 3) products falling within CN codes 2207 20 00 and 2905 11 00 (ethanol) which are not of synthetic origin, 4) products produced from biomass, including products falling within CN codes 4401 and 4402 (certain wood products). This (largely CHECK) corresponds to the definition of biofuels in Directive 2003/30/EC.

<sup>15</sup> OJ C 37 of 3.2.2001, p.3.

<sup>16</sup> OJ C28 of 1.2.2000, p.2

friendly inputs in comparison to conventional production processes. The aid component should be limited to neutralising the effects of the additional costs and should be subject to a periodic review at least every five years. Since the aid only concerns biofuels which without aid would not be competitive in the market and since the aid level is reviewed annually, the notified aid scheme complies with these conditions. In addition, when assessing environmental aid granted both to sectors covered by Annex I and to sectors outside the scope of this Annex, it may appear justified to treat all sectors in the same way. In fact, the Commission previously accepted such equal treatment in certain cases<sup>17</sup>

- (20) According to section E.3.3 of the Community Guidelines, operating aid in favour of the production of renewable energy will usually be allowable. The Commission takes the view that such aid qualifies for special treatment because of the difficulties these sources of energy have sometimes encountered in competing effectively with conventional sources.
- (21) The definition of biofuels that Lithuania uses is in line with the definition used in Article 2(a) of Directive 2001/77/EC<sup>18</sup>. Therefore, the biofuels are also renewable energy sources within the meaning of point 6 of the Community Guidelines.
- (22) Point 56 of the Community Guidelines lays down that operating aid must be limited to cover the difference between the cost of producing energy from renewable energy sources and the market price of that energy. This implies that the production costs of the energy produced from renewable energy sources taking into account the aid should thus not be below the market price of a comparable energy obtained from fossil energy sources for which not aid is granted. This is further developed in points 59 and 60 of the Community Guidelines.
- (23) According to Lithuania, biofuels are not competitive with fossil fuel because the costs of producing biofuel exceed those of fossil fuel. The duty reduction is aimed at helping to offset the additional production costs of biofuels. From the tables below, which are based on the information provided by Lithuania, it is clear that the aid enables producers to sell the blended fuel at a price that is just sufficient to compete with fossil fuel.
- (24) The table below contains comparative information concerning biodiesel.

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<sup>17</sup> e. g. Commission decision on the German Ecotax, NN47/99, OJ C166 of 12.6.199, p. 2 and N575/A/99, OJ C322 of 11.11.2000, p. 9.

<sup>18</sup> Directive 2001/77/EC of the European Parliament and the Council of 27 September 2001 on the promotion of electricity produced from renewable energy sources in the internal market, OJ L 283 of 27.10.2001, p.33. Article 2 (a) of this directive lists the following renewable energy sources: wind, solar, geothermal, wave, tidal, hydropower and biomass, landfill gas, sewage treatment plant gas and biogases. Article 2 (b) lays down that biomass shall mean the biodegradable fraction of products, waste and residues from agriculture (including vegetal and animal substances), forestry and related industries, as well as the biodegradable fraction of industrial and municipal waste.

**Table 2: Costs and price of blended biodiesel compared to fossil fuel**

<b>LTL<sup>19</sup> /litre</b>	<b>Biodiesel</b>	<b>Diesel</b>
1. Raw material (+)	1,35	0,69
2. Processing (+)	0,47	0,03
3. Other (laboratory test, reorganisation of production) (+)	0,26	
4. Production costs	2,08	0,72
5. Logistic (+)	0,24	0,20
6. By-product selling price (-)	0,42	
7. Pre-tax costs	1,90	0,92

<b>LTL /litre blended diesel</b>	<b>3% RME in blend</b>	<b>5% RME in blend</b>
Costs of RME in blend (3% x 1,9 LTL/litre); (5% x 1,9 LTL/litre)	0,06	0,10
Cost of fossil diesel (97% x 0,92LTL/litre); (95% x 0,92LTL/litre)	0,89	0,87
Cost of blending		
Excise (97% x 0,85 LTL/litre); (95% x 0,85 LTL/litre)	0,82	0,81
Total (Sales price of blend)	1,77	1,78
Correction for lower energy content blended (13%) <sup>20</sup>	0,01	0,01
<b>Sales price blended biodiesel (conditional)</b>	<b>1,78</b>	<b>1,79</b>

Cost of fossil diesel (100% x 0,92 LTL/litre)	0,92
Excise for fossil diesel	0,85
<b>Sales price fossil fuel<sup>21</sup></b>	<b>1,77</b>

- (25) The table above reflects the basic comparison of blended biodiesel costs and fossil fuel. The sales price for blended biodiesel with 3–5 % RME is estimated at 1,78 – 1,79 LTL/litre and is a result of cost of biofuel (3-5% RME) added with costs of fossil fuel (97-95% volume in final blend) reduced with excise duty exemption (for 3-5%RME)

<sup>19</sup> The exchange rate applied is the following: 3.4528 LTL = 1 EUR.

<sup>20</sup> Due to the lower energy value of biodiesel in comparison to fossil diesel, the consumption of biodiesel is estimated to be 13% higher than the consumption of fossil diesel.

<sup>21</sup> VAT is not included in the calculations, since this affects the prices proportionately and does not change the conclusion that the total production costs of biodiesel and bioethanol including reduced excise duty are above the market price of fossil diesel and petrol including excise duty.

added with excise for the fossil fuel part. Excise duty reduction for blended diesel with 3-5% RME amounts to 0,025 LTL/litre.

- (26) The sales price for blended biodiesel is compared to the fossil fuel price including excise duty which amounts to 1,77 LTL/litre. It is obvious that the price of biofuel is higher than the price of fossil fuel and it can be concluded that there is no overcompensation. If costs of blending were included in the calculation, the risk of overcompensation would be even smaller.
- (27) A similar calculation was made for bioethanol blend. Regarding the Republic of Lithuania Law on Biofuel, Bio Motor Fuels and Bio-Oils of 5 February 2004, fossil petrol (octane 95 petrol) has to be blended with ETBE in proportion of 7% minimum and 15% maximum. Since only 47% of one litre of ETBE is derived from biomass, the blend will contain 3.29% - 7.05% of bioethanol respectively.

**Table 3: Costs and price of blended bioethanol compared to fossil fuel**

LTL/litre	Bioethanol	Petrol
1. Raw material (+)	[...]*	[...]
2. Processing (+)	[...]	[...]
3. Other (laboratory test, reorganisation of production) (+)	[...]	[...]
4. Production costs	[...]	[...]
5. Logistic (+)	[...]	[...]
6. By-product selling price (-)	[...]	[...]
7. Pre-tax price	[...]	[...]

LTL /litre blended petrol	3,29% ethanol in blend	7,05% ethanol in blend
Costs of ETBE in blend (3.29% x 1,80 LTL/litre); (7.05% x 1,80 LTL/litre)	[...]	[...]
Cost of fossil petrol (96.71% x 0,88 LTL/litre); (92.95% x 0,88LTL/litre)	[...]	[...]
Cost of blending	[...]	[...]
Excise (96.71%, x 0,98LTL/litre) ; (92.95% x 0,98LTL/litre)	[...]	[...]
Total (Sales price of blend)	[...]	[...]
Correction for lower energy content (65%) <sup>22</sup>	[...]	[...]
Sales price blended petrol (conditional)	[...]	[...]

Cost of fossil petrol (100% x 0,88)	0,88
Excise for fossil petrol	0,98
Sales price fossil fuel	<b>1,86</b>

- (28) The sales price for blended bioethanol with 3.29 – 7.05 % ethanol is estimated at [...] LTL/litre. The excise duty reduction for blended petrol with ETBE 7% - 15% (or 3.29% - 7.05% ethanol) amounts to 0.032 LTL/litre. The sales price for fossil fuel amounts to

<sup>22</sup> Bioethanol has about 65% of the calorific value of petrol.

\* Business secrets

1,86 LTL/litre which is below the market price of bioethanol blend. The Commission finds no undue advantage in the upper and lower thresholds below/above which the aid level will not be adjusted. Moreover, if costs of blending were included in the calculation, the risk of overcompensation would be even smaller.

- (29) On the basis of this data, the production costs of biodiesel and bioethanol are above the market price of fossil fuels. The Commission thus considers that the excise duty exemption does not overcompensate for the extra production costs of biofuels.
- (30) Apart from bioethanol and biodiesel the notified measure also foresees that pure vegetable oil can benefit from the tax reduction. The Lithuanian authorities estimate that production costs of biodiesel, produced from pure vegetable oil amounts to 2,08 LTL/litre (excluding VAT), which is considerable above the threshold of fossil diesel (1,77 LTL/litre).
- (31) Lithuania committed itself to carrying out an analysis, as soon as a biofuel product concerned will benefit from the tax reduction, to ensure that the reduction will not lead to overcompensation. This information will also be submitted to the Commission in the annual monitoring reports.
- (32) Lithuania intends to introduce the exemption on the basis of the Directive 2003/96/EC on energy taxation and within the limits of Article 16 of this directive which allows Member States to apply a reduced excise duty and exemptions for products derived from biomass subject to certain conditions.
- (33) Considering the above, the Commission concludes that the aid is restricted to covering the difference between the cost of producing energy from renewable energy sources and the market price of that energy and that there is no overcompensation in the meaning of the Community Guidelines.
- (34) Lithuania has committed itself to providing annual monitoring reports to the Commission. Finally, the Commission notes that the duration of the measure is limited to five years starting from the adoption of the present decision until 31.12.2010.
- (35) The Commission comes to the conclusion that the notified aid measure fulfils the conditions laid down in the Community guidelines on State aid for environmental protection. The Commission thus holds that the measure can be exempted from the general prohibition of State aid pursuant to Article 87(3) (c) of the EC Treaty.

#### **IV. DECISION**

The Commission has accordingly decided not to raise objections against the notified measure, since it fulfils the conditions to be considered compatible with the EC Treaty.

If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen 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://ec.europa.eu/community/state\\_aids/](http://ec.europa.eu/community/state_aids/).

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

European Commission  
Directorate-General for Competition  
Directorate for State Aid  
B-1049 Brussels

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Yours faithfully,

For the Commission

Neelie Kroes  
Member of the Commission