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Fuel tax exemption in the fisheries sector

Legal arguments supporting a large elimination of those exemptions

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1 Executive summary

1. The ETD currently provides for the exemption of taxation of fuel in the maritime sector.
2. The current position of the European Commission is favourable to the elimination of the fuel tax exemption in the revised version of the ETD.
3. Some voices raised that such elimination of the fuel tax exemption would not be in line with the UNCLOS (including Article 89 of the UNCLOS providing that “No State may validly purport to subject any part of the high seas to its sovereignty.”)
4. We consider that arguments exist to refute any invalid extraterritorial effect of the application of the revised ETD to international waters:

- Vessels flying the flag of an EU member State cannot withdraw themselves from the application of the (revised) EU Directive: a vessel remains bound by the laws of its flag State when it enters international waters.
- Vessels flying the flag of a non EU member state: the criteria of the port where the non-EU vessel is fueling could be used as a valid connecting factor (in line with the case law rendered in the aviation sector in which the airport of destination is recognised as a valid connecting factor)

5. We consider that irrespective of the conformity of the revised ETD with the UNCLOS, no direct effect can be invoked, so that an individual / company could not validly invoke such alleged non conformity:

- The UNCLOS does not have a direct effect as a whole
- In particular, Article 89 of the UNCLOS does not have a direct effect

6. Efforts that have been set up by the International Maritime Organization ('IMO') to reduce greenhouse gas emissions on a global scale

- International global market based measures are however slow processes and a comparison with the aviation sector shows that the need for a large international consensus generally leads to less ambitious decisions being taken.
- However, the practice shows that the adoption of strong regulation at the EU level, even if debated, speeds up the process at the international level to agree on a balanced global market based measure

2 Factual Background

2.1 Energy Taxation Directive on fuel taxation for ships (including fishing purposes)

Article 14.1.c of the Council **Directive 2003/96/EC** of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity (hereafter the Energy Taxation Directive, in short "ETD") states the following:

> *1. In addition to the general provisions set out in Directive 92/12/EEC on exempt uses of taxable products, and without prejudice to other Community provisions, Member States **shall exempt the following from taxation** under conditions which they shall lay down for the purpose of ensuring the correct and straightforward application of such exemptions and of preventing any evasion, avoidance or abuse:*
>
> *[…]*
>
> *(c) energy products supplied for use as **fuel** for the purposes of navigation within **Community waters** (including **fishing**), other than private pleasure craft, and electricity produced on board a craft.*

2.2 Commission position on revising the ETD

The current position of the European Commission is favourable to the elimination of the tax exemption in the revised version of the ETD:[1]

1. Divergent national rates in combination with a wide range of tax exemptions and reductions, which are essentially forms of fossil fuel subsidies, are currently applied to safeguard the competitiveness of the EU industries. These exemptions are **not in line with the European**

[1] European Commission, Inception Impact Assessment (Ref. Ares (2020)1350088 – 04/03/2020), notably on page 2.

Green Deal. Furthermore, the majority of energy taxation occurs in the field of road transport, which leads to a fragmentation of the internal market and distorts the level playing field between the road, maritime and aviation sector.

2. There is a **lack of alignment between the ETD and the EU Emission Trading System, the Renewables Directive and the Energy Efficiency Directive**: no promotion of energy efficiency, cleaner fuels or greenhouse gas emissions reduction. Once again, not in line with the European Green Deal.

3. The minimum tax rates introduced by the ETD have lost their effect and no longer contribute to the proper functioning of the internal market. This is due to the absence of an indexation mechanism and the fact that most EU Member States tax the majority of energy products (incl. electricity in some cases) considerably above the ETD minimum tax rates.

This is also reflected in the Commission Staff Working Document,[2] in which the European Commission states that the current exemption put at risk the environmental objectives:

> *In addition, according to Article 14 of the ETD Member States must exempt from taxation energy products supplied for use as fuel for the purpose of air navigation other than in private pleasure-flying and energy products supplied for use as fuel for the purposes of navigation within Community waters (including fishing), other than private pleasure craft, and electricity produced on board a craft, which potentially contradicts the decarbonisation objectives of the EU transport policy as well as EU climate objectives. The strong growth of air traffic has caused air transport emissions to more than double in the last years. Aviation activities have been included in the **EU ETS**, but in order to further support the process led by the International Civil Aviation Organisation (ICAO) and allow for an agreement at global level on a "Carbon Offsetting and Reduction Scheme for International Aviation" (**CORSIA**), the EU has limited the EU ETS to flights within the European Economic Area (EEA), applies equal treatment to all operators on those routes and grants free emission allowances covering about 85% of the activity covered by the EU ETS.*
>
> *For international maritime, global efforts to limit emissions are led by the International Maritime Organisation (IMO). IMO adopted in April 2018 an initial strategy to reduce greenhouse gas emissions from ships. The strategy defines an emission reduction objective of at least 50% reduction by 2050 compared to 2008 annual emissions coupled with a vision for the decarbonisation of the sector.*
>
> *Moreover, the mandatory tax exemptions for air navigation and navigation within Community waters may distort the level playing field in the transport sector.*

2.3 Potential violation of the United Nations Convention on the Law of the Seas ('UNCLOS')[3]

One could argue that such elimination of fuel tax exemption could be limited/challenged on the basis that no State may take jurisdiction on any part of the high seas.

[2] European Commission, SWD (2019) 329 final.
[3] United Nations Convention on the Law of the Sea (UNCLOS), signed at Montego Bay on 10 December 1982, which entered into force on 16 November 1994 and was approved by Council Decision 98/392/EC of 23 March 1998 (OJ 1998 L 179, p. 1).

This principle is indeed recognised in Article 89 of the UNCLOS:

> *"Article 89 Invalidity of claims of sovereignty over the high seas*
>
> *No State may validly purport to subject any part of the high seas to its sovereignty."*

The present note provides a first assessment of the arguments that could be raised towards this position, and therefore in favour of the legality to eliminate the exemption of fuel taxes.

3 Can the elimination of fuel tax exemption be applied to international waters

3.1 Case study - EU case law on ETS in the aviation sector

The extra-territoriality of EU regulations have led to major discussions in the aviation sector, and in particular in respect of the scope of application of the Emission Trading Scheme ("ETS") within the aviation sector.[4]

Seized in the context of a preliminary question, the European Court of Justice rendered a judgment[5] in relation to the legal powers of the EU to extend the scope of application of the ETS to segments of international flights when these arrived or departed from EU airports.

The claimants (including the Air Transport Association of America) were considering that applying the ETS (and thus imposing a financial obligation to air carriers outside of the borders of the European Union) was contradicting, inter alia, principles of customary international law. Among those principles:

> *"(b) the principle of customary international law* ***that no State may validly purport to subject any part of the high seas to its sovereignty****;*
>
> *(c) the principle of customary international law of freedom to fly over the high seas;*
>
> *(d) the principle of customary international law (the existence of which is not accepted by the Defendant) that aircraft overflying the high seas are subject to the exclusive jurisdiction of the country in which they are registered, save as expressly provided for by international treaty"*[6]

This analysis is particularly useful for considering the situation of non-EU vessels operating in EU waters and refuelling in EU ports.

After confirming the obligation of the European Union to respect international law (including the principles of customary international law cited above), the ECJ tends to confirm that tight connecting factors can be used as a proper basis for jurisdiction:

The principle:

> *"123. The European Union must respect international law in the exercise of its powers, and therefore Directive 2008/101 must be interpreted, and its scope delimited, in the light of the relevant rules of*

[4] Directive 2008/101/EC of the European Parliament and of the Council of 19 November 2008 amending Directive 2003/87/EC so as to include aviation activities in the scheme for greenhouse gas emission allowance trading within the Community (OJ 2009 L 8, p. 3).
[5] Court of Justice, 21 December 2011, C-366/10, Rec. 2011, I -3755.
[6] Court of Justice, 21 December 2011, C-366/10, Rec. 2011, I -3755, paragraph 45

the international law of the sea and international law of the air (see, to this effect, Poulsen and Diva Navigation, paragraph 9)".[7]

The connecting factors:

"124. On the other hand, European Union legislation may be applied to an aircraft operator when its aircraft is in the territory of one of the Member States and, more specifically, on an aerodrome situated in such territory, since, in such a case, that aircraft is subject to the unlimited jurisdiction of that Member State and the European Union (see, by analogy, Poulsen and Diva Navigation, paragraph 28).

125. In laying down a criterion for Directive 2008/101 to be applicable to ***operators of aircraft registered in a Member State or in a third State*** *that is founded on the fact that* ***those aircraft perform a flight which departs from or arrives at an aerodrome situated in the territory of one of the Member States****, Directive 2008/101, inasmuch as it extends application of the scheme laid down by Directive 2003/87 to aviation,* ***does not infringe the principle of territoriality or the sovereignty which the third States*** *from or to which such flights are performed have over the airspace above their territory, since those aircraft are physically in the territory of one of the Member States of the European Union and are thus subject on that basis to the unlimited jurisdiction of the European Union."*[8]

3.2 Connecting factors for the application of the revised ETD

3.2.1 Vessel flying an EU flag

Different criteria can be invoked in favour of the application of the revised ETD to international waters.

Vessels flying the flag of an EU member State cannot withdraw themselves from the application of the (revised) EU Directive. Such statement derives from international maritime law, and particularly in the (customary) rule that a vessel remains bound by the laws of its flag State when it enters international waters: **this also includes national laws on fuel taxation, unless a national law would explicitly exclude maritime fuel from its scope of application**.[9]

Such rule follows from Articles 91, 92 and 94 of the UNCLOS:

Article 91 UNCLOS:

1. Every State shall fix the conditions for the grant of its nationality to ships, for the registration of ships in its territory, and for the right to fly its flag. ***Ships have the nationality of the State whose flag they are entitled to fly****. There must exist a* ***genuine link*** *between the State and the ship.*

2. Every State shall issue to ships to which it has granted the right to fly its flag documents to that effect.

Article 92 UNCLOS:

1. Ships shall sail under the flag of one State only and, save in exceptional cases expressly provided for in international treaties or in this Convention, ***shall be subject to its exclusive jurisdiction on***

[7] Court of Justice, 21 December 2011, C-366/10, Rec. 2011, I -3755, paragraph 123.
[8] Court of Justice, 21 December 2011, C-366/10, Rec. 2011, I -3755, paragraphs 124 and 125.
[9] Articles 91 & 92 UNCLOS

***the high seas**. A ship may not change its flag during a voyage or while in a port of call, save in the case of a real transfer of ownership or change of registry.*

2. A ship which sails under the flags of two or more States, using them according to convenience, may not claim any of the nationalities in question with respect to any other State, and may be assimilated to a ship without nationality.

Article 94 UNCLOS (United Nations Convention on the Law of the Sea):

*1. **Every State shall effectively exercise its jurisdiction and control in administrative, technical and social matters over ships flying its flag.***

*2. In particular every State shall: (a) maintain a register of ships containing the names and particulars of ships flying its flag, except those which are excluded from generally accepted international regulations on account of their small size; and (b) **assume jurisdiction under its internal law over each ship flying its flag and its master, officers and crew in respect of administrative, technical and social matters concerning the ship. […]***

Based on the above, one can invoke that:

- A vessel can only have one flag State, being the State of registration.
- A vessel always remains under the jurisdiction and control of its flag State in international waters.
- A vessel will always have to observe the laws of its flag State in international waters, including its taxation laws.

3.2.2 Vessel flying a non EU flag

It is more complex to determine a valid connecting factor applying to non-EU vessels, which would enable the EU to apply the revised ETD to international waters.

However, we consider that the **criteria of the port where the non-EU vessel is fuelling could be used**.

This would – in our opinion – be in line with the developments of the Advocate General developed in the ETS case.[10] In this case, the Advocate General considers that it is valid to take into account, for the calculation of the quotas to be surrendered by any airline (whether from the EU or from a third country), not only the part of the flight operated within the EU but the entire flight (i.e. over third countries and over the high seas), to the extent that there is a proper connecting factor. Similarly, the EU could consider in respect of the revised ETD that the criteria of the port in which a vessel is fuelling is sufficient to consider that the elimination of tax fuel exemption will apply.

The reasoning of the Advocate General in the ETS case is the following:

"On the absence of any extraterritoriality effect of the EU emissions trading scheme:

145. As many of the governments and institutions involved in the proceedings have correctly concluded, Directive 2008/101 does not contain any extraterritorial provisions. The activities of

[10] Opinion of the Advocate General Kokott delivered on 6 October 2011 in Case C-366/10.

airlines within the airspace of third countries or over the high seas are not made subject to any mandatory provisions of EU law by virtue of this directive. In particular, Directive 2008/101 does not give rise to any kind of obligation on airlines to fly their aircraft on certain routes, to observe specific speed limits or to comply with certain limits on fuel consumption and exhaust gases.

146. Directive 2008/101 is concerned solely with aircraft arrivals at and departures from aerodromes in the European Union, and it is only with regard to such arrivals and departures that any exercise of sovereignty over the airlines occurs: depending on the flight, these airlines have to surrender emission allowances in various amounts, and if they fail to comply there is a threat of penalties, which might even extend to an operating ban.

147. The fact that the calculation of emission allowances to be surrendered is based on the whole flight in each case does not bestow upon Directive 2008/101 any extraterritorial effect. Admittedly, it is undoubtedly true that, to some extent, account is thus taken of events that take place over the high seas or on the territory of third countries. This might indirectly give airlines an incentive to conduct themselves in a particular way when flying over the high seas or on the territory of third countries, in particular to consume as little fuel as possible and expel as few greenhouse gases as possible. However, there is no concrete rule regarding their conduct within airspace outside the European Union.

148. ***It is by no means unusual for a State or an international organisation also to take into account in the exercise of its sovereignty circumstances that occur or have occurred outside its territorial jurisdiction****. The principle of worldwide income thus applies in many countries under income tax law. Under antitrust law as well as in merger control it is normal worldwide practice for competition authorities to take action against agreements between undertakings even if those agreements have been concluded outside the territorial scope of their jurisdiction and may perhaps even have a substantial effect outside that scope of jurisdiction. In one fisheries case, the Court of Justice even ruled that fish caught in the high seas could be confiscated as soon as the vessel concerned, flying the flag of a third country, reached a port within the European Union.*

149. ***The decisive element from an international law perspective is that the particular facts display a sufficient link with the State or international organisation concerned****.* ***The particular connecting factor can be based on the territoriality principle, the personality principle or – more rarely – on the universality principle****."*

[…]

154. The territoriality principle does not prevent account also being taken in the application of the EU emissions trading scheme of parts of ***flights that take place outside the territory of the European Union****. Such an approach reflects the nature as well as the spirit and purpose of environmental protection and climate change measures. It is well known that* ***air pollution knows no boundaries and that greenhouse gases contribute towards climate change worldwide irrespective of where they are emitted****; they can have effects on the environment and climate in every State and association of States, including the European Union.*

155. A comparison with the aforementioned fisheries case[11] is also worthwhile in this context. If it is permissible under the territoriality principle for fish caught outside the European Union to be confiscated from a vessel sailing under the flag of a third country whilst at a port within the European

[11] Reference is made to the Poulsen and Diva Navigation case

Union, there cannot be any prohibition against exhaust gases from an aircraft emitted outside the airspace of the European Union being taken into account on its departure from or arrival at an aerodrome within the European Union for the purposes of calculating the emission allowances to be surrendered."[12]

The Advocate General has taken the stance that in terms of environmental protection, European regulations can have an effect on areas beyond the European Union.

4 Can the UNCLOS be invoked to oppose the elimination of fuel tax exemption in the revised ETD

Would the revised ETD not be in line with the UNCLOS, another question is to determine if an individual or a company is validly entitled to invoke it to its benefit.

4.1 The UNCLOS has no direct effect as a whole

In order for an individual or a company to effectively challenge the validity of the elimination – by the EU - of fuel exemption above the limits of 12/200 miles, one has to demonstrate that the UNCLOS[13] - or one or several relevant provisions of UNCLOS - has a direct effect.

The UNCLOS does not have, as a whole, a direct effect, as it is clearly stated by both the ECJ[14] and the European Commission:

"*49.* [However,] *in the Intertanko case the Court of Justice examined UNCLOS and held that* ***private litigants are not entitled to rely on its provisions to challenge the validity of EU legislation****. The Court of Justice held that the nature and the broad logic of UNCLOS shows that* ***this convention is not intended to apply directly and immediately to individuals and to confer upon them rights or freedoms capable of being relied by states****. The Court of Justice, looking at the overall structure and purpose of UNCLOS, decided that this UN convention was primarily intended to lay down rights and duties between states as to the various uses of the seas, within different maritime zones agreed in the convention.* ***Even insofar as these provisions may seem to grant rights to ships, in the view of the Court of Justice, such rights are primarily derived from states who grant their flag to ships and thus have assumed an obligation to supervise these ships and their crew and to ensure the application and enforcement of certain (agreed) rules on board the c o vessels flying their flag.***

50. ***Consequently, the Intertanko judgment excludes direct effect for UNCLOS as a whole****."*[15]

[12] Opinion of the Advocate General Kokott delivered on 6 October 2011 in Case C-366/10
[13] United Nations Convention on the Law of the Sea (UNCLOS), signed at Montego Bay on 10 December 1982, which entered into force on 16 November 1994 and was approved by Council Decision 98/392/EC of 23 March 1998 (OJ 1998 L 179, p. 1).
[14] Case C-308/06, 3 June 2008, Intertanko
[15] Observation of the European Commission in Case C-366/10, Paragraphs 49 and 50.

It is therefore established that an individual or company cannot invoke – generally – the direct application of the UNCLOS. To the contrary, it has to demonstrate that a specific provision of UNCLOS can endorse a direct effect.

4.2 Article 89 of the UNCLOS has no direct effect

Besides the absence of general direct effect of the UNCLOS, we have assessed whether Article 89 of UNCLOS has a direct effect and could therefore be raised by individuals/companies to challenge the legality of the elimination of fuel exemption.

As a recall, Article 89 of the UNCLOS provides that:

> *"Article 89 Invalidity of claims of sovereignty over the high seas*
>
> *No State may validly purport to subject any part of the high seas to its sovereignty."*

The ECJ case law as well as the position of the European Commission are clearly opposed to a direct effect of Article 89 of the UNCLOS:

> *"Clearly this* [absence of direct effect] *must also apply to Articles 89 and 87(b) of UNCLOS, provisions that are, it should be noted, expressis verbis directed to States only. Consequently, the Court of Justice cannot assess the validity of the ETS Directive in the light of these provisions of UNCLOS. These principles may not be invoked directly to impugn EU legislation. Otherwise, the Claimants would be able to circumvent the strict conditions set out in the Court of Justice's case-law for provisions of international conventions to which the EU is a party."*[16]

An individual or company cannot invoke the direct application of Article 89 of the UNCLOS.

5 Efforts at the International Maritime Organization

In the Commission Staff Working Document regarding the revision of the ETD, the Commission refers to the efforts that have been set up by the International Maritime Organization ('IMO') to reduce greenhouse gas emissions on a global scale.[17]

IMO itself has however not yet adopted a proper initiative to set up an actual, global taxation scheme for fuel of vessels, which would make unsustainable fishing economically unattractive. In early 2021, the Marshall and Solomon Islands, who have considerable influence in the IMO due to their strategic maritime position, launched a proposal within the IMO to introduce a global levy of USD$100/ton of greenhouse gases for vessels.[18]

[16] Observation of the European Commission in Case C-366/10, Paragraph 50.
[17] For a brief overview, see: https://www.imo.org/en/MediaCentre/HotTopics/Pages/Reducing-greenhouse-gas-emissions-from-ships.aspx.
[18] See for example: https://lloydslist.maritimeintelligence.informa.com/LL1136097/Marshall-Islands-demands-$100-tax-on-shipping-emissions.

This proposal will be brought up for consideration at the next meeting of the IMO Marine Environment Protection Committee, which is taking place in this month of June 2021.

A successful debate or a global consensus that emissions from fuels should be taxed will entail an important step towards making sure that, in any case, long distance fishing fleets operating in international waters will not be able to evade fuel taxation.

International global market based measures are however slow processes and a comparison with the aviation sector shows that the need for a large international consensus generally leads to less ambitious decisions being taken.

However, the practice shows that the adoption of strong regulation at the EU level, even if debated, speeds up the process at the international level to agree on a balanced global market based measure. Indeed, the adoption of the ETS in the aviation sector has led to a lot of legal (and political) debates but clearly led to an acceleration of the adoption of the CORSIA system at the international level.

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