

BIOFUELS

May 2006

a) Background

The frameworks for biofuel production and tax treatment are set out in Decree-Law 62/2006 of 21 March and Decree-Law 66/2006 of 22 March respectively.

The first decree-law transposes Directive 2003/30/EC of the European Parliament and of the Council of 8 May, which indicates that Member States should actively promote the production and use of biofuels in order to increase energy independence and diversification within the Community, on the one hand, and to reducing CO₂ emissions, which is vital for attaining the Community's environmental goals, on the other.

The second decree-law, in exercise of the legislative powers conferred by the 2006 State Budget Law, establishes the rules for tax benefits which will enable biofuels to become more competitive in relation to fossil fuels (crude oil derivatives, mainly diesel and petrol).

The legislature has created a partial exemption (reduction) from the special duty on petroleum products (ISP) for these quantities, as follows:

Current taxation on diesel (per thousand litres)

| | Diesel | Biodiesel |
|----------|---------|------------|
| ISP Rate | €339.41 | €39.41 (*) |

(*) The rate may be reduced by the Government to an amount of not more than €39.41

Current taxation on petrol (per thousand litres)

| | Petrol | Bioethanol |
|----------|---------|-------------|
| ISP Rate | €557.95 | €257.95 (*) |

(*)The rate may be reduced by the Government to an amount of not more than €257.95

b) Partial exemption from ISP

(Duty on Petroleum Products)

In order to achieve the set national and community objectives, the following market shares for biofuels were laid down for Portugal:

Percentage values

| YEAR | 2006 | 2007 | 2008 | 2009 | 2010 |
|--------|------|------|------|------|------|
| Diesel | 2 | 3 | 5.75 | 5.75 | 5.75 |
| Petrol | 2 | 3 | 5.75 | 5.75 | 5.75 |

Total values (in millions of litres)

| YEAR | 2006 | 2007 | 2008 | 2009 | 2010 |
|--------------|------------|------------|------------|------------|------------|
| Diesel | 114 | 171 | 320 | 320 | 320 |
| Petrol | 46 | 69 | 130 | 130 | 130 |
| Total | 170 | 240 | 450 | 450 | 450 |

c) Companies benefiting from the exemption

The companies which will produce the partially-exempt biofuels will be selected for a period of not more than six years by means of a public tender or the "authorisation mechanism".

- The selection criteria are the following:
- A continuing supply of biofuel (multi-annual contracts);
- Maintaining sufficient reserves; and
- Incorporating endogenous agricultural products as raw material (cf. Resolution of the Council of Ministers 11/2004 of 22 January).

d) Transferring quantities between biofuels

It remains unclear as to whether the Government, on agricultural, industrial or commercial grounds, will permit the amount of biofuel destined for blending with petrol to be "transferred" to diesel instead, if this were to become necessary. It is, however, likely that this procedure will be authorised.

e) Best-placed companies

Since the production of biofuels bears similar characteristics, in certain cases, to that of the production of cooking oils, companies in this sector which intend to change or diversify their activity are ideally positioned to break into this new area of industrial production.

f) But what exactly are biofuels anyway?

Biofuels, as the name suggests, are fuels derived from organic matter, particularly rape, sunflowers, artichokes and plant waste, which can be added to diesel (e.g. biodiesel) or petrol (e.g. MTBE - Methyl tert-butyl ether) in ratios of not more than 5%, and which release less greenhouse gases, such as CO₂.

The biofuels added to diesel and petrol, up to this ratio, are burned normally by all automobiles without any need to make adjustments to the engines (for example, 2% biodiesel has been added to diesel fuel in France ever since the nineteen eighties).

g) Total ISP exemption for small specialised producers

Apart from the partial ISP exemption aimed at medium-sized and large industrial production as mentioned above, a full ISP exemption is envisaged for small specialised producers, subject to the restriction that the exemption may not exceed a national total of 15,000,000 kilos per annum.

A small specialised producer is one whose annual biofuel production level does not exceed 3,000,000 kilos and whose production, based on pre-existing business agreements, is destined for companies, cooperatives or groups of companies. This biofuel is not sold on the conventional fuel market and vehicles are supplied solely from pumps located on the premises of the transport company using the biofuel.

As this particular measure is aimed at company fleets, that is to say, vehicles belonging to one single entity, it enables the vehicles to use normal diesel blended with around 20% biodiesel after "adjustments" have been made to the engines, thus providing tax gains for the transport company as well as environmental gains for the community.

h) The tax status of the biofuel production centre

Biofuel factories have the tax status of transformation tax warehouses and will have to register with the Directorate-General for Customs and Excise Duties (DGAIEC). The obligations that the DGAIEC requires companies holding this tax status to comply with are significantly less rigid. ■

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