FACTUAL RECORD

Law of Sulfur Content in Diesel

Secretaría para las Solicitudes sobre Asuntos de Cumplimiento Ambiental
Acuerdo de Promoción Comercial (APC) Perú-EEUU

Secretariat for Submissions on Environmental Enforcement Matters
United States-Peru Trade Promotion Agreement (TPA)

Secretariat for Submissions on Environmental Enforcement Matter United States - Peru Trade Promotion Agreement
Submitted to the Environmental Affairs Council in accordance with Article 18.9, paragraph 5, of the United States – Peru Trade Promotion Agreement

FACTUAL RECORD

Law of Sulfur Content in Diesel

Sumbitter: [names are kept confidential in accordance with Article 8 of the Understanding for Implementing Article 18.8 of the United States – Peru Trade Promotion Agreement] | Party: Perú | Submission N°: SACA-SEEM/PE/002/2019

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INITIALS AND ACRONYMS: (CONSIDERING TERMS IN SPANISH)

ECA	Environmental Cooperation Agreement established in the TPA
TPA	Trade Promotion Agreement US-Perú
CONAM	National Environmental Council
Comptroller	Office of the Comptroller General of the Republic
Council	Environmental Affairs Council established in the TPA
Ombudsman	Ombudsman´s Office
Understanding	Understanding to implement Article 18.8 of the TPA
INC	Índex of Noxiousness of Fuels
ISC	Selective Consumption Tax
Law of Sulfur Content in Diesel	Law No. 28694, which regulates the sulfur content in diesel fuel
Law of Creation of the Ministry of the Environment	Legislative Decree No. 1013, Law of Creation, Organization and Functions of the Ministry of the Environment
LGA	General Environmental Law
MEF	Ministry of Economy and Finance
MINAM	Ministry of the Ambiente
MINEM	Ministry of Energy and Mines
OEA	Organization of American States
Party/Parties	Refers either to one or both countries (Peru and USA)
Solicitantes	Peruvian citizens that filed the submission addressed in the Factual Record: Submission SACA-SEEM/PE/002/2019
TUO de la Ley del IGV e ISC	Single Ordered Text of the Law of General Sales Tax and Selective Consumption Tax

I. THE SECRETARIAT AND THE ENVIRONMENTAL AFFAIRS COUNCIL

I.1. I.1.The Secretariat for Submissions on Environmental Enforcement Matters

- The Secretariat for Submissions on Environmental Enforcement Matters was established through the Understanding for Implementing Article 18.8 of the United States – Peru Trade Promotion Agreement (Understanding).
- According to the Understanding, its functions are the following:

1. Perform the functions established for it under Articles 18.8 and 18.9 of the United States – Peru Trade Promotion Agreement (TPA). In particular, the Secretariat shall:

    (a) receive and consider public submissions in accordance with paragraphs 1 and 2 of Article 18.8;

    (b) request a Party to respond to public submissions in accordance with paragraph 4 of Article 18.8, receive the Party's response in accordance with paragraph 5 of Article 18.8, and consider the submission and any response provided by the Party in accordance with paragraph 1 of Article 18.9;

    (c) inform the Environmental Affairs Council (Council), in light of any response provided by the Party, whether public submissions warrant developing a factual record, in accordance with paragraph 1 of Article 18.9;

    (d) prepare factual records when any member of the Council instructs it to do so, submit them to the Council and, if directed by a member of the Council, make them available to the public, in accordance with Article 18.9;
    and may take such additional actions as are appropriate to carry out the functions established in Articles 18.8 and 18.9 of the TPA.

2. The Secretariat shall apply working and other procedures that the Council establishes for considering public submissions, preparing factual records, engaging experts, preparing reports to the Council, protecting confidential information, making documents publicly available, or other matters related to its functions.

I.2. The Environmental Affairs Council

- The Council was established by Article 18.6 of the TPA, and according to the Article 18.6.2, its functions are the following:

  (a) consider and discuss the implementation of Chapter 18 of the TPA;

  (b) provide periodical reports to the Free Trade Commission regarding the implementation of Chapter 18 of the TPA;

  (c) provide for public participation in its work, including by:

    (i) establishing mechanisms to exchange information and discuss matters related to the implementation of Chapter 18 of the TPA with the public;
    (ii) receiving and considering input in setting the agenda for Council meetings; and
    (iii) receiving public views and comments on the issues the public considers relevant to the Council's work and requesting public views and comments on the issues the Council considers relevant to its work;

  (d) consider and discuss the implementation of the Environmental Cooperation Agreement (ECA) signed by the Parties, including its work program and cooperative activities, and submit any comments and recommendations, including comments and recommendations received from the public to the Parties and to the Environmental Cooperation Commission established under the ECA;

  (e) endeavor to resolve matters referred to it under Article 18.12.4; and

  (f) perform any other functions as the Parties may agree.

II. SUBMISSIONS AND FACTUAL RECORDS

II.1. Process of receipt and consideration of submissions

- Any person of a Party to the TPA may file a submission with the Secretariat for Submissions on Environmental Enforcement Matters (Secretariat) asserting that a Party is failing to effectively enforce its environmental laws, in accordance with Article 18.8.1 of the TPA.
- On June 9, 2015, the Parties signed the Understanding that established the Secretariat. A Memorandum of Understanding (MOU) was also signed with the Organization of American States (OAS) by which it was agreed that the OAS will house and provide administrative and technical support to the Secretariat in its headquarters in Washington D.C., in the United States.
- The Secretariat, among its main functions, receives and considers submissions filed by any person, natural or legal, of a Party, in accordance with the provisions of Article 18.8 of the TPA.
- The Secretariat may consider a submission where the Secretariat determines the submission meets the criteria set out in paragraph 2 of Article 18.8 of the TPA. Where a submission meets these criteria, the Secretariat shall determine whether the submission merits requesting a response from the Party, in accordance with paragraph 4 of Article 18.8 of the TPA.
- In accordance with Article 18.9.1 of the TPA, if the Secretariat considers that the submission, in light of any response provided by the Party, warrants developing a factual record, shall so inform the Council and provide its reasons.
- The Secretariat shall prepare a factual record if any member of the Council instructs it to do so.
- The Secretariat shall submit a draft factual record to the Council. Any Party may provide comments on the accuracy of the draft within 45 days thereafter. Afterwards, the Secretariat shall incorporate, as appropriate, any such comments in the final factual record and submit it to the Council. The Secretariat shall make the final factual record publicly available, normally within 60 days following its submission, if any member of the Council instructs it to do so.

II.2. Preparation of the factual record

- For the preparation of a factual record, according to Article 18.9.4 of the TPA, the Secretariat shall consider any information provided by a Party and may consider any relevant technical, scientific, or other information:

  (a) that is publicly available;
  (b) submitted by interested persons;
  (c) submitted by national advisory or consultative committees;
  (d) developed by independent experts; or
  (e) developed in accordance with the ECA.

III. EXECUTIVE SUMMARY

- **Date of submission:** July 25, 2019.
- **Submitters:** [names are kept confidential in accordance with Article 8 of the Understanding for Implementing Article 18.8 of the United States - Peru Trade Promotion Agreement.]
- **Assertion:** That the Peruvian Government has failed to effectively enforce Article 3 of Law No. 28694, which regulates the sulfur content in diesel fuel.
- **Date of instruction to prepare the factual record:** October 1, 2020.
- **Date of submission of the draft factual record to the Council:** September 10, 2021.
- **Date of consultation done by the Secretariat to the Parties on the relationship between the draft version of the factual record and its final version:** May 20, 2022.
- **Date of last response of a Party to the consultation done by the Secretariat on the relationship between the draft version of the factual record and its final version:** July 1, 2022.
- **Date of submission of the revised draft factual record to the Council:** August 22, 2022.
- **Date of submission of the final version of the factual record to the Council:** October 24, 2022.
- **Date of presentation of the factual record done by the Executive Director to the Council:** November 30, 2022.
- **Date of receipt of instructions to make public the factual record:** December 19, 2022.
- **Summary of the facts:**

  1. Five Peruvian nationals who requested that the Secretariat keep their personal information confidential (the submitters), filed a submission with the Secretariat via email on July 25, 2019, asserting that the Peruvian Government failed to effectively enforce Article 3 of Peruvian Law No. 28694, which regulates the sulfur content in diesel fuel (Law of Sulfur Content in Diesel).

2. On March 20, 2006, the Congress of the Republic of Peru enacted the Law of Sulfur Content in Diesel. Article 3 of the aforementioned law is titled "Tax measures to promote clean fuels".

3. Article 3 of the Law of Sulfur Content in Diesel established that the Peruvian Government must gradually, starting on January 1, 2008, determine the Selective Consumption Tax (ISC) on fuels, introducing the criterion of proportionality to the degree of noxiousness of the pollutants that these fuels contain for the health of the population.

4. Likewise, it is noted that the Peruvian Government must, through the Ministry of Economy and Finance (MEF) in coordination with the Ministry of the Environment (MINAM), annually approve the indices of relative noxiousness that will be used to determine the ISC.

5. In addition to this, it is stated that the Peruvian Government must conclude the gradual restructuring of the criterion of proportionality for the degree of noxiousness, and fully consider the criterion of noxiousness in the taxation of fuels by no later than January 1, 2016, when the taxation of fuels will fully consider the criterion of noxiousness.

IV. SCOPE OF THE FACTUAL RECORD

1. The instruction received from two members of the Council for the preparation of a factual record for Submission SACA-SEEM/PE/002/2019, included below, does not include any additional scope beyond that proposed by the Secretariat in Notification SACA-SEEM/PE/002/2019/N1 recommending the preparation of this factual record; as it can be verified as follows:

Instruction to the United States-Peru Trade Promotion Agreement Secretariat for Submissions on Environmental Enforcement Matters Regarding Submission SACA-SEEM/PE/002/2019 Asserting that the Government of Peru is Failing to Effectively Enforce Article 3 of Law No. 28694, Law that regulates the sulfur content in diesel fuel.

THE UNITED STATES OF AMERICA:

SUPPORTIVE of the process provided for in Articles 18.8 and 18.9 of the *United States-Peru Trade Promotion Agreement* (PTPA) regarding Submissions on Enforcement Matters and the preparation of factual records;

CONSIDERING Submission SACA-SEEM/PE/002/2019 (the "Submission") filed by five Submitters of Peruvian citizenship who identified their personal information as confidential (hereinafter, the "Submitters") on July 25, 2019, and the Responses provided by the Government of Peru on June 1, 2020;

HAVING REVIEWED the Secretariat's July 13, 2020 Notification in accordance with Article 18.9(1) of the PTPA, informing the Environmental Affairs Council that the Secretariat considers the Submission to warrant the development of a Factual Record; and

PURSUANT to Article 18.9(2) of the PTPA,

HEREBY INSTRUCTS the Secretariat to prepare a factual record concerning the Submission.

John Thompson
Acting Deputy Assistant Secretary of State
Bureau of Oceans and International Environmental and Scientific Affairs
U.S. Department of State

Kelly Milton
Assistant U.S. Trade Representative for Environment and Natural Resources
Office of the U.S. Trade Representative

U.S. Representatives on the PTPA Environmental Affairs Council

2. In accordance with paragraphs 41, 42, 43, 44, 45 and 47 of Notification SACA- SEEM/PE/002/2019/N1, the scope of this factual record is:

41. In this regard, it is important to highlight that the mandatory and specific legal requirement of Article 3 of Law No. 28694, which is also precisely the central subject of Submission No. SACA-SEEM/PE/002/2019, consists of the Peruvian Government annually approving the indices of noxiousness of fuels from the year 2008 to 2016 inclusive.

42. According to the available information, the Peruvian Government determined the indices of noxiousness of the 2014-2015 and 2018-2019 periods, which is the reason for Article 3 of Law No. 28694 not being effectively enforced in the annual approval of the indices of noxiousness of fuels for the years: 2008, 2009, 2010, 2011, 2012, 2013, 2016, 2017 and so far in 2020 .

43. Additionally, Article 3 of Law No. 28694 requires that the approval of the indices of noxiousness of fuels be gradually adjusted every year. The aforementioned gradual adjustment would not have occurred because no indices of noxiousness of fuels was approved in most years since 2008 that would allow such gradual adjustment to be determined.

44. In addition, Article 3 of Law No. 28694 requires that, as of January 1, 2016, the gradualness in the indices of noxiousness of fuels cease, and that, from that date onwards, the criterion of noxiousness be fully considered.

45. Lastly, the final section of Article 3 of Law No. 28694, establishes that as of 2016 the taxes levied on fuels fully considers the criterion of noxiousness. Therefore, it is important to mention that the ISC is not the only tax levied on fuels, which requires the analysis of whether these other taxes, such as the general sales tax, road tax and import duties, have been considered in the restructuring to which Article 3 of Law No. 28694 refers.

46. Having taken into consideration the response of the Peruvian Government, the Secretariat considers that the Submission contains central issues that must be addressed and developed in further detail. Therefore, the Secretariat recommends the development of the Factual Record regarding the effective enforcement of Article 3 of Law No. 28694, Law that regulates the sulfur content in diesel fuel. The Factual Record will be developed taking into consideration the regulatory steps taken by the Peruvian Government in its response to the Secretariat.

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1 In Notification SACA- SEEM/PE/002/2019/N1, the original text of Article 3 of Law No. 28694 that contains the phrase “índices de nocividad” was translated as “index of noxiousness,” changing the term “índices” (plural) to “index” (singular). In this final version of the factual record, “índices” is translated as “indices” thus preserving the original language of the law.

2 It must be said that in August 2020, Supreme Decree No. 007-2020-MINAM approved the INC for the 2020-2021 period.

V. THE SUBMISSION PROCESS FOR SACA-SEEM/PE/002/2019/PE

V.1. Submission – Article 18.8.1 of the TPA

1. The submitters filed a submission with the Secretariat via email dated July 25, 2019, asserting that the Government of Peru is failing to effectively enforce Article 3 of the Law of Sulfur Content in Diesel.

2. Article 3 of the Law of Sulfur Content in Diesel establishes:

> ***"Article 3.- Taxation measures to promote clean fuels***
> *The Selective Consumption Tax on fuels will be determined on a gradual basis, starting on January 1st, 2008, by introducing the criterion of proportionality into the degree of noxiousness that fuel pollutants have on the health of the population. To this end, the Ministry of Economy and Finance, in coordination with the National Environmental Council (CONAM), will annually approve the indices of relative noxiousness that will be used. This restructuring must be gradually carried out until January 1st, 2016, at the latest, when the taxation of fuels will fully consider the criterion of noxiousness."*

V.2. Determination in accordance with Article 18.8.1 and 18.8.2 of the TPA

3. On October 18, 2019, the Secretariat issued Determination SACA-SEEM/PE/002/2019/D1 that determined the submission met the criteria set out in Article 18.8.2 of the TPA.

4. The Secretariat established that the submission was written in Spanish and was filed by five natural persons from Peru. The submission included documentary evidence, as well as an exhaustive identification of the law that the Peruvian Government was asserted to be failing to effectively enforce. The submission appeared to be focused on promoting the effective enforcement of the Party's environmental laws and did not give any indication of seeking to harass an industry. It also provided information on a written communication by the submitters addressed to a relevant institution of the Party.

V.3. Determination in accordance with Article 18.8.4

5. On April 2, 2020, the Secretariat issued Determination SACA-SEEM/PE/002/2019/D2, determining that the submission merited requesting a response from the Party. The Secretariat considered that, among other things, the submission was not frivolous, asserted potential harm to the submitters, addressed matters that would contribute to achieving the objectives of Chapter 18 of the TPA and the ECA, and was not exclusively drawn from media reports.

V.4. Response from the Government of Peru

6. On June 1, 2020, the Government of Peru responded, as requested by the Secretariat. In its response, the Government of Peru noted the following, in relation to the substantive aspects in this submission[3]:

   (a) MINAM updates the Indices of Noxiousness of Fuels (INC) based on technological changes and official information available on inventoried emission sources, the physical-chemical characteristics of fuels (density, the calorific value, sulfur content, biofuel content, among others), energy consumption by productive sector and by type of fuel.

   (b) The last INC approved for the 2018-2019 period remained valid until its update, that is, it does not expire. In this regard, the Government of Peru states that the Constitution, the Constitutional Court and the majority of legal scholars ("doctrina mayoritaria" in Spanish) support what has been said so far regarding that these indices were neither modified nor suspended nor repealed by another legal norm. For this reason, the Peruvian Government is in compliance with the provisions of Article 3 of the Law of Sulfur Content in Diesel.

   (c) The Party's response states that through Ministerial Resolution No. 412-2019-MINAM, published on January 5, 2020, the pre-publication in the Official Legal Gazette El Peruano of the Supreme Decree draft that would approve the INC for the 2020-2021 period was done in order to know the opinions and/or suggestions of the interested parties. As of the date that the Government of Peru presented its response, this regulation was in the internal process of being approved.

   (d) The ISC levied on fuels derived from petroleum is determined following the provisions of Article 61 of the Single Ordered Text[4] of the General Sales Tax and Selective Consumption Tax, TUO of IGV and ISC Law (approved by Supreme Decree No. 055-99-EF and modifications to its regulations) respecting the ranges established by said article; as well as using the tax policy guidelines approved by the Peruvian Government through the respective Multiannual Macroeconomic Frameworks as reference. According to these guidelines, the ISC is determined based on the criterion of negative externality generated by the consumption of affected goods.

   (e) The Party's response emphasizes that the ISC was included as a criterion in the Declaration of the Principles of Fiscal Policy 2006-2008 for the first time as a result of the publication of the Law of Sulfur Content in Diesel. The Declaration makes the following point regarding the ISC:

> *"A redirection of consumption based on criteria for the protection of health and/or the environment will be sought."*

(f) Likewise, the Government of Peru states that the INC is one of the criteria used to determine the ISC applicable to fuels, which is indicated in the Technical Report No. 801-2013-DGCA-VMGA/MINAM. Among these additional criteria to determine the tax burden of the ISC on fuels, the following are noted: - the use of oil and derivatives in the national chains of production, the effects of the variation in fuel prices on inflation and the prices of goods and essential services, and their impact on the majority of the population, the impact of the variation in fuel prices on the competitiveness of key massive economic sectors and key market segments, as is the case of electricity rates, or the cost of passenger and cargo transportation, among others, which could later have effects on the generation of jobs and on tax collection. The Party's response points out that the ISC on fuels has a dual purpose: tax and non-tax, as well as effects on other indices such as inflation, competitiveness, and job creation. The Party's response states that the consideration of the INC in the determination of the ISC allows the structuring of the tax burden of fuels based on their noxiousness, which results in a valuation of the negative externality generated by the consumption of said goods.

(g) It is specified that the INC does not establish direct values related to the amount of the ISC, as it is MEF's competence to establish criteria of proportionality in distributing the ISC on gaseous, liquid, and solid fuels. MEF establishes the criteria of proportionality according to the ranges provided by Article 61 of the TUO of the IGV and ISC Laws and uses the tax policy guidelines regarding the ISC as a reference, regardless of the amount that can be established as the base tax, thus redirecting the consumption of the most polluting fuels by encouraging the use of clean fuels.

(h) The criterion of negative externality, it is noted, is an exclusive characteristic of the ISC that is not present in the structure of the other taxes regulated by national laws.

(i) The Government of Peru points out that the objective of the Law of Sulfur Content in Diesel, with regards to the tax implications of the Law's Article 3, is to use the ISC—which aims to assess the negative externality generated—as a way for users of polluting fuels to begin to internalize damage caused to the population's health, and promote the use of less polluting fuels, which would bear a lower tax burden for this tax.

3 The procedural and conceptual aspects presented as part of the different documents presented by the Government of Peru have been analyzed by the Secretariat in a separate document that has been made known to both Parties.
4 Official version of a legal norm that has been subject to different modifications.

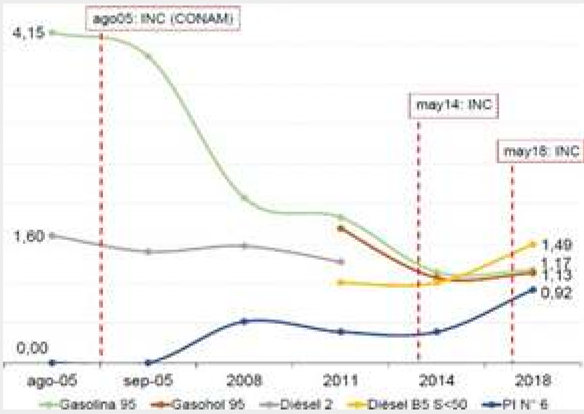
(i) The Government of Peru points out that the objective of the Law of Sulfur Content in Diesel, with regards to the tax implications of the Law's Article 3, is to use the ISC—which aims to assess the negative externality generated—as a way for users of polluting fuels to begin to internalize damage caused to the population's health, and promote the use of less polluting fuels, which would bear a lower tax burden for this tax.

(j) The Party's response states that although Supreme Decree No. 211-2007-EF established a schedule with the fixed amounts of the ISC for fuels determined based on noxiousness until 2016, the tax set out in said schedule is to be taken as a reference, representing the desired direction towards which the tax policy tends in relation to updating the ISC on fuels. This schedule does not represent a commitment to an annual modification of said tax.

(k) From the first publication of the INC in 2005, and subsequent publications of the INC in 2014 and 2018, the determination of the ISC has taken noxiousness as a reference, incorporating these indices with the goal to determine the impact on the consumption of fuels according to the toxicity of each one. Thus, the application of the tax policy in relation to the ISC, shows that the most noxious fuels (such as Industrial Oil No. 6) were modified with an upward trend, while the less noxious fuels (such as Gasoline 95 and, later, Gasohol 95), were modified with a downward trend.

(l) In this regard, the figure below is attached:

Graphic No. 1:
Evolution of ISC of representative fuels and INC
(Soles per gallon)



(m) It is specified that not updating new indices of noxiousness has not prevented the tax policy guidelines regarding the ISC from being followed for the purpose of structuring the tax burden of fuels based on their noxiousness.

(n) Additionally, the Government of Peru mentions the approval of a set of norms it approved related to the prohibition of use and sale of diesel with sulfur, to vehicle emissions, vehicle scrapping; all of which, as noted, respond to the objective established in Article 18.1 of the TPA, related to the approval of laws and policies that provide for and encourage high levels of environmental protection.

(o) Based on the aforementioned points, it is concluded that the Peruvian Government has effectively implemented Article 3 of the Law of Sulfur Content in Diesel regarding the annual approval of the indices of noxiousness of fuels. Likewise, it is noted that the taxes levied on fuel consumption have been modified according to the toxicity of each one.

V.5. Notification in accordance with Article 18.9.1

7. On July 13, 2020, the Secretariat sent a Notification in accordance with Article 18.9.1 to the Council, informing that the Secretariat considered that the submission warranted the development of a factual record.

V.6. Instruction for the preparation of the factual record

8. On October 1, 2020, the United States instructed the Secretariat to prepare a factual record for Submission SACA-SEEM/PE/002/2019.

V.7. Draft factual record

9. On September 10, 2021, the Secretariat sent the draft factual record to the Council for Submission SACA-SEEM/ PE/002/2019, in compliance with the instruction received on October 1, 2020, and in accordance with the provisions of paragraph 5 of Article 18.9 of the TPA

V.8. Comments from the Parties on the draft factual record

10. In accordance with paragraph 5 of Article 18.9 of the TPA, the Government of Peru submitted comments to the draft factual record on October 21, 2021. In addition to the aspects addressed in item V.4.6. of this document, the Peruvian Government noted the following in this communication regarding the substantive aspects:

(a) The Peruvian Government asserts that it has not failed to enforce the provisions of Article 3 of the Law of Sulfur Content in Diesel. In particular, the Party's response mentions the following:

- The Decree of the Directive Council No. 018-2005-CONAM-CD (December 2, 2005) which was valid until May 1, 2014.

- Supreme Decree No. 006-2014-MINAM (May 1, 2014) was in effect until May 9, 2018, when Supreme Decree No. 003-2018-MINAM was approved.

(b) By Supreme Decree No. 007-2020-MINAM, dated August 18, 2020, the INC (indices of noxiousness) corresponding to the 2020-2021 period had been approved. This regulation was subject to pre-publication in the Official Gazette El Peruano through Ministerial Resolution No. 412-2019-MINAM, dated December 31, 2019, in order to know the opinions and/or suggestions of the interested parties with the aim of giving guarantee to the right of citizen participation in environmental matters.

(c) The Peruvian Government asserts that it is not appropriate to include other taxes other than the ISC since it was not part of the notification, as well as for the lack of supporting information from the submitters and the Secretariat, and for technical reasons. In turn, it states that none of the bills debated in Congress that comprise the legislative background of the Law of Sulfur Content in Diesel make any reference to the other taxes set forth by the submitters and the Secretariat.

V.9. Consultation on the relationship between the draft version of the factual record and its final version

11. On May 20, 2022, the Executive Director of the Secretariat sent a query to the Points of Contact (POC) regarding a procedural matter in relation to the scope of Articles 18.9.6 and 18.9.7 of the TPA, noting that the Secretariat has made various requests for access to information regarding the present case, and therefore it was considered necessary to incorporate said new information into the final version of the factual record.

It was therefore expected that there could be a substantive difference between the draft version presented to the EAC on September 10, 2021, and the final factual record.

12. On June 7, 2022, the representative of the Government of Peru, in regard to the Secretariat's query, noted that to the extent that the factual record is still in process, the final version of said document could differ from its draft version, by incorporating changes before submitting a final version to the Council. Likewise, it was noted that in the case of new information, it was considered important that the new information be made known to the Parties so that they can present their comments before submitting the final factual record to the Council. According to the Government of Peru, this would allow the safeguarding of due process and the right of defense.

13. On July 1, 2022, the U.S. Government answering to the consultation done by the Secretariat noted their agreement with the representatives of Peru in that the final version of the factual record may differ from the version submitted to the Council on September 10, 2021. The United States noted that the final factual record should reflect what the Secretariat considers relevant and important from appropriate sources, including the Parties. Regarding the submission of a second draft version of the factual record, the POCs of the U.S. Government noted a subsequent review of the draft is not contemplated in the TPA; however, taking into consideration the unique circumstances related to the turnover in the Executive Director position, the United States agreed that with the Secretariat preparing a second version of the draft factual record, if it is substantially changed as a result of having included new information or having omitted information that had been previously included. It is due to the unique situation caused by the change in Executive Directors that the Parties should, in this instance, have the opportunity to comment on the accuracy of the new information included in the revised draft factual record. However, it is noted that from their point of view, the Parties are not authorized to comment for a second time on information that has not been changed in the revised draft factual record.

14. Taking account these opinions, on August 28, 2022, the Secretariat forwarded the revised preliminary version of the factual record to the Council, granting a period of 45 days to provide comments on the accuracy of its contents.

15. On October 6, 2022, the Secretariat received comments from both the Government of the United States and the Government of Peru, which have been analyzed and incorporated, as appropriate, in this final factual record.

V.10. Publication of the final version of the factual record

16. The Secretariat presented the final factual record in the session of the Council dated November 30, 2022.

17. On December 19, 2022, the Secretariat received instructions from two of the representatives of the US Government to make publicly available this final factual record.

VI. FACTS RELATED TO THE SUBMISSION

The purpose of this factual record is to analyze the facts related to the subject of the submission that asserts the lack of effective enforcement of Article 3 of the Law of Sulfur Content in Diesel Fuel. Under this premise, in this section, three major issues are addressed: the first refers to the regulations on fuel quality in force before the approval of the Law of Sulfur Content in Diesel; the second refers to the scope of said legal regulation; and the third refers to its implementation.

VI.1. Regulation on fuel quality in force before the approval of Law 28694

VI.1.1. Regulation of National Standards of Environmental Air Quality. Supreme Decree No. 074-2001-PCM

1. A first antecedent of regulation related to the quality of fuels in the Peruvian environmental law is found in the 2001 Regulation of National Standards of Environmental Air Quality, approved through Supreme Decree No. 074-2001-PCM[5].

2. This Regulation, which was the first law that regulated environmental standards in Peru, includes as a first aspect to be considered in the development of the Action Plans for the improvement of air quality a topic related to the "continuous improvement of the quality of fuels"[6].

VI.1.2. INC for the 2005-2006 period. Decree of the Directive Council No. 018-2005-CONAM-CD

3. The first law that regulated the INC in Peru was a regulation approved by CONAM in 2005.[7]

5 This legal norm was published in the Official Gazette El Peruano on June 2, 2001.
6 Regulation of National Standards of Environmental Quality of the Air. Supreme Decree No. 074-2001-PCM. Article 10, paragraph (a)
7 This legal norm was published in the Official Gazette El Peruano on December 2, 2005.

4. In its recitals, the regulation indicates that CONAM, in its capacity as National Environmental Authority, had prepared the INC with the purpose of informing citizens, in general, and fuel consumers, in particular, about these indices allowing the comparison of environmental toxicity and noxiousness generated by the different types of fuels. This law also mentions the guarantee of the right to environmental information. The last recital in this law even noted that:

   "...it is necessary to disseminate and consider the impact of fuels on health and the environment, taking into account the amount of pollutants produced by each fuel and the toxicity each of the pollutants has on humans."

5. This same regulation established that the Climate Change and Air Quality Unit of CONAM was responsible for carrying out the annual updating of the INC in coordination with the sectors involved.

6. It should be noted that Annex 2 of this law, called "Methodology for the definition of the INC", noted the following in relation to the periodicity of the approval of the INC:

   "This index is expected to evolve, updating it every year as new or more detailed information is generated (specifically in relation to emission factors by category and by pollutant)."
   (emphasis our own)

VI.2. Scope of Article 3 of the Law of Sulfur Content in Diesel

VI.2.1 Validity, regulation, and purpose of the Law of Sulfur Content in Diesel

7. The Law of Sulfur Content in Diesel, which entered into force the day after its publication; that is, on March 23, 2006, per the provisions of Article 109 of the Political Constitution of Peru, which states that "The law comes into force the day following its publication in the official gazette, unless a provision of the same law delays its effect in whole or in part". In the present case, the law did not establish the postponement of its validity.

8. It is pertinent to point out that, in the Sole Transitory and Final Provision of the Law of Sulfur Content in Diesel, it was established that "[by] means of a supreme decree endorsed by the Ministers of Energy and Mines and of Economy and Finance, the regulation of this Law will be approved, in a period not exceeding ninety (90) days after its enactment". To date, no specific regulatory standard that develops the scope of this law has been approved, without prejudice to the fact that regulatory development standards have been approved under the same law.

9. The Law of Sulfur Content in Diesel, in fulfilling its purpose, declared the regulation of sulfur levels contained in diesel fuel to be of public necessity and a national priority to safeguard air quality and public health.

VI.2.2 The Origins of the Law of Sulfur Content in Diesel

10. To better understand the scope of the Law of Sulfur Content in Diesel, documentary sources related to the formulation and approval process of this legal standard have been identified.

11. There were five bills of law that were integrated into the opinion of the Energy and Mines Commission that later became the Law of Sulfur Content in Diesel (Bills 12089, 12130, 12152, 12719 and 12798/2004-CR).

12. These bills were reviewed, and it was identified that the only one that presented specific content related to the indices of noxiousness of fuels was Bill 12130/2004-CR presented on December 10, 2004, by Congressman Luis Heysen Zegarra (Aprista Peruano Party).

13. This bill was called "Bill of law that proposes that the Ministry of Energy and Mines force fuel market agents, especially refineries, to reduce excess sulfur in derivatives, such as diesel and gasoline, a situation that seriously affects the health of the population".

14. In the explanatory memorandum of this bill, the following was stated in relation to the indices of noxiousness:

"...it is necessary to encourage the use of clean fuels, that is, those that do the least damage to the environment, and discourage the use of those fuels that, due to their toxic emissions, cause serious damage to the environment, affecting the health and quality of life of people.
It is also necessary to adapt the tax policy to encourage the consumption of clean fuels to improve air quality, by levying taxes, through the Selective Consumption Tax, on a greater proportion of dirty fuels or on those that are more polluting for the environment. This process of changing to using clean fuels should not have an effect on the tax cash flow nor on the economics of producers, importers, sellers or consumers, and therefore a reasonable period of time must be provided so that the necessary adjustments can be made both in the collection of taxes and in actions of adaptation that must be taken to be able to produce, import, sale and make use of less polluting fuels."

15. The following proposals on the matter were included within the legal formula[8] of this bill:

> ***"Article 2.- Selective Consumption Tax (ISC) and Clean Fuels***
> The Selective Consumption Tax levied on the sale of fuels must reflect the negative externalities, as well as the relative social cost that each fuel produces when it evaporates after its combustion. Consequently, the calculation of the ISC applied under the specific system must consider an index of relative noxiousness that will be set annually by CONAM..."

> ***"Article 3.- Noxiousness Factor and the ISC***
> The Ministry of Economy and Finance will use the Noxiousness values...established by CONAM, to set the minimum values of the Selective Consumption Tax that correspond to each fuel."

16. The aforementioned Opinion of the Energy and Mines Commission approved by the Commission on April 27, 2005, stated the following regarding the indices of noxiousness of fuels:

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8 Legal formula refers specifically to the texts of the articles of a legal norm.

> *"…the proposal to establish mechanisms to promote clean fuels through the reduction of the amount of the ISC is accepted.*
> *…it is proposed that a legal formula be approved that will not create or increase public spending, but rather will generate the benefit of promotional measures encouraging the consumption of clean fuels.*
> *Although these provisions will reduce the amount of tax collected, they will provide a counterweight by reducing the polluting effects derived from the combustion of sulfur in the urban environment, which will also result in public investment savings in health, which will lead to improving the population's standard of living.*
> *The replacement project focuses on Diesel fuel because it is the one that maintains alarming levels of sulfur content."*

17. With this text, the substitute text contained in the Opinion of the Energy and Mines Commission, collected the following legal formula:

> ***"Article 3.- Taxation measures to promote clean fuels***
> The Selective Consumption Tax on fuels will be determined on a gradual basis, starting on January 1st, 2008, by introducing the criterion of proportionality into the degree of noxiousness that fuel pollutants have on the health of the population. To this end, the Ministry of Economy and Finance, in coordination with the National Environmental Council (CONAM), will annually approve the indices of relative noxiousness that will be used. This restructuring must be gradually carried out until January 1st, 2016, at the latest, when the taxation of fuels will fully consider the criterion of noxiousness."

18. This Opinion was presented and debated in the Permanent Commission of the National Congress on July 20, 2005. In this regard, the relevant interventions that appear in the Diary of Debates of the Congress of the Republic have been identified, which are presented below:

DIARY OF DEBATES
LEGISLATIVE PERIOD 2004-2005
PERMANENT COMMISSION
7th SESSION
(Morning session)
WEDNESDAY, JULY 20, 2005
"Unanimous opinion of the Energy and Mines Commission, with a substitute text for Bills No. 12089, 12130, 12152, 12719 and 12798/2004-CR, which proposes declaring the regulation of sulfur levels contained in diesel fuel to be of public necessity and a national priority, to safeguard air quality and public health.
The CHAIRMAN (Jorge Mera Ramírez).— The Chairman of the Commission, Congressman Heysen Zegarra, has the floor for up to ten minutes.
Mr. HEYSEN ZEGARRA (PAP).—[9]"
"...an important issue within this bill of law that is being presented for the consideration of the Permanent Commission is the content of Article 3, which speaks of tax measures to promote clean fuels.
We know, and I think it is essential that we all be aware, that we have a tax system based on the collection of taxes levied on fuels, and that the system has prioritized that single criterion, leaving aside another that could be introduced, with respect to gradually considering the index of noxiousness of fuels.
This proposal contained in Article 3, which we sent to the Permanent Commission, in no way intends to affect the tax cash flow which, as we well know, depends primarily on fuel taxes.[10]"
"Mr. HEYSEN ZEGARRA (PAP).—...
What I have proposed is that the criterion of noxiousness of fuels be introduced for the determination of the selective consumption tax, and that this criterion, which is gradually introduced, be fully in force in 2016; that is, that the gradualness ends in that year. That does not mean that the selective consumption tax on fuels will be eliminated, ...
Therefore, what we are trying to propose here is to introduce a criterion that reflects the gradual and progressive elimination of the perverse incentives to use dirty fuels that seriously harm the health of the population; a new criterion that will correct this situation that has lasted 30 years, for which we give a term of ten years. In conclusion, that the criterion of the index of noxiousness of fuels be introduced to fine-tune the levels of

9 Congress of the Republic of Peru. Diary of Debates of the Permanent Commission (2004-2005 period). p.128
10 Congress of the Republic of Peru. Diary of Debates of the Permanent Commission (2004-2005 period). p.129
11 Congress of the Republic of Peru. Diary of Debates of the Permanent Commission (2004-2005 period). p.134

the selective consumption tax on fuels .[11]”
“Mr. HEYSEN ZEGARRA (PAP).— .... This bill does not establish tax rates or place a straitjacket on the selective consumption tax; therefore, it does not put the balance of the tax cash flow at risk. The only thing this bill indicates is to introduce the criterion of the index of noxiousness so that the Ministry of Economy, when proposing the amounts of the selective consumption taxes on the different fuels, takes that criterion into account as well, and not only that of the balance of the tax cash flow, which obviously will always continue...[12]”
“In this bill, there is no restriction or straitjacket, nor are fees set. It is only noted to introduce the criterion of the index of noxiousness so that, when it sets the selective consumption taxes on fuels, it does not continue to maintain perverse incentives for dirty fuels; but, on the contrary, introduce favorable incentives, progressively and gradually, to protect the population's health, which determine that the dirtiest fuels pay —let's say— the current levels and the cleanest fuels pay less, but maintaining the balance of the tax cash flow.
Therefore, there is no way that the balance of the tax cash flow can be put at risk or affect the multi-year macroeconomic framework through this project....[13]”

19. As a result of the debate, the following is the text that was finally approved in the scope of the Permanent Commission (on the same day, July 20, 2005) and which was included in the Law of Sulfur Content in Diesel:

***Artículo 3°**.- **Medidas de promoción de combustibles limpios**---*
Gradualmente, a partir del 1 de enero de 2008, se determinará el Impuesto Selectivo al Consumo a los combustibles, introduciendo el criterio de proporcionalidad al grado de nocividad por los contaminantes que éstos contengan para la salud de la población. Para tal efecto, el Ministerio de Economía y Finanzas en coordinación con el Consejo Nacional del Ambiente – CONAM aprobarán anualmente los índices de nocividad que serán utilizados. Esta reestructuración deberá realizarse de forma gradual hasta el 1 de enero de 2016 como máximo, fecha en que la tributación que grava los combustibles, considerará plenamente el criterio de nocividad.--

12 Congress of the Republic of Peru. Diary of Debates of the Permanent Commission (2004-2005 period). p.147
13 Congress of the Republic of Peru. Diary of Debates of the Permanent Commission (2004-2005 period). p.148

20. It should be noted that the Enrolled Bill of this Law received observations from the Executive Branch and was sent to the Congress of the Republic on August 15, 2005, through Official Letter No. 080-2005-PR, but none of such observations questioned Article 3 in particular. In any case, it should be noted that the Congress of the Republic approved modifications based on the observations from the Executive Power, after which, the Law of Sulfur Content in Diesel was enacted.

21. Lastly, it should be noted that no reference to taxes other than the ISC has been found in the legislative history of the law under analysis, as was indicated by the submitters. This is why there is no documentary basis to assert that the concept of "taxation" indicated in the last section of Article 3 of the Law of Sulfur Content in Diesel could be interpreted as including different taxes than the ISC.

VI.2.3 Environmental regulatory framework and policies in which the Law of Sulfur Content in Diesel is framed

22. To understand the regulatory context in which Article 3 of the Law of Sulfur Content in Diesel is framed, as well as its implementation, we present below the regulations that are referred in the recitals and in the explanatory memorandum of the regulations issued by MINAM to establish the INC.

Chart No. 1:
Environmental legislation mentioned in the norms issued by MINAM about INC

LEGAL INSTRUMENT	DATE	ENVIRONMENTAL LAWS REFERRED TO IN THE RECITALS AND THE EXPLANATORY MEMORANDUM OF THE NORMS ISSUED BY MINAM ABOUT INC
Supreme Decree No. 006-2014-MINAM. The INC is approved for the 2014-2015 period.	May 1, 2014	- Political Constitution, Article 2, paragraph 22 - General Environmental Law, Law No. 28611: Article VI of the Preliminary Title, Articles 3, sub-paragraph g of Article 11, and Articles 33.4 and 75 - Political Constitution, Article 2, paragraph 22 - Framework Law for the National System of Environmental Management, Law No. 28245: Article 5.
Supreme Decree No. 003-2018-MINAM. The INC is approved for the 2018-2019 period.	May 9, 2018	- Political Constitution, Article 2, paragraph 22 - General Environmental Law, Law No. 28611: Article 1 of the Preliminary Title, Article 3, sub-paragraph g of Article 11.
Supreme Decree No. 007-2020-MINAM. The INC is approved for the 2020-2021 period.	August 18, 2020	- Political Constitution, Article 2, paragraph 22 - General Environmental Law, Law No. 28611: Article 1 of the Preliminary Title, Article 3, sub-paragraph g of Article 11.

23. From the above table we can identify the environmental regulations that have been repeatedly referred to when noting the legal grounds for the formulation of the INC by MINAM. Its main contents are presented below:

- Article 2 of the Political Constitution (1993) recognizes the fundamental rights of the human person. In particular, paragraph 22 states that every person has the right: "... to a balanced and appropriate environment for the development of [their] life.

- The General Environmental Law (LGA), Law No. 28611 (2005), which is the coun try's main environmental law, states the following in Article I of its Preliminary Title:

“Article I.- Of the fundamental right and duty. Every person has the inalienable right to live in a healthy, balanced, and appropriate environment for the full development of life, and the duty to contribute to effective environmental management and to protect the environment, as well as its components, particularly ensuring the health of people individually and collectively, the conservation of biological diversity, the sustainable use of natural resources and the sustainable development of the country”.

- At the same time, Article 3 of the LGA notes the role the Government has in environmental matters, emphasizing that the Government "designs and applies the policies, laws, instruments, incentives and sanctions that are necessary to guaran tee the effective exercise of the rights and compliance with the obligations and responsibilities contained in this Law.”

- Lastly, sub-paragraph g) of Article 11 of the LGA mentions the need to articulate and integrate tax matters with the objectives of environmental protection and sustainable development as one of the basic environmental guidelines of public policies.

24. In addition to the aforementioned, the LGA also contains relevant provisions regarding the relationship between taxation and the environment, which is established in the following articles:

- ***Article 4.- Taxation and the environment***
  The design of the national tax framework considers the objectives of the National Environmental Policy, particularly promoting environmentally responsible behaviors, responsible production and consumption methods for goods and services, the conservation, sustainable use, and recovery of natural resources, as well as the development and use of appropriate technologies and clean production practices in general.
- ***Article 36.- Economic instruments***
  In accordance with the Government budgetary and tax regulatory framework, public entities at the national, sectoral, regional, and local levels incorporate economic instruments, including taxes, in the exercise and scope of their respective functions to encourage environmentally sound practices and compliance with the objectives of the National Environmental Policy and environmental regulations.

25. Regarding the policy framework, the Law of Sulfur Content in Diesel was approved in 2006, when there was still no explicit public policy on environmental matters, even though basic environmental guidelines for public policy did exist in the LGA (Article 11).

26. In 2009, the first environmental policy of Peru was approved, through Supreme Decree No. 012-2009-MINAM of May 23, 2009, where the following was stated:

POLICY AREA 2 COMPREHENSIVE MANAGEMENT OF ENVIRONMENTAL QUALITY
3. AIR QUALITY
Policy Guidelines
a) Establish measures to prevent and mitigate the effects of air pollutants on people's health. (…)
c) Encourage the modernization of the automotive fleet by promoting instruments, use of means of transport and fuels that contribute to reducing the levels of atmospheric pollution.

27. On July 25, 2021, the current National Environmental Policy to 2030 was approved by Supreme Decree No. 023-2021-MINAM, which states the following regarding air quality:

Causes of the public problem:
(…)
b) Deterioration of environmental quality, which is the alteration of the physical, chemical and biological properties of air, water, and soil, which generates damage to the development of ecosystems that provide goods and services, which directly impact health of people…Air pollution in cities is responsible for significant annual mortality and morbidity rates, largely as a result of heart and lung disease.
(…)
Priority objective 3: Reduce air, water and soil pollution
This objective responds to the direct cause of the "Deterioration of environmental quality". The aim of this Objective is to … reduce the levels of morbidity and mortality ,…in respiratory diseases at the national level. This Objective also responds to the need to improve air quality…in the country's hydrographic units.…

28. It is appropriate to note here that the environmental institutional framework has had an important development in Peru in recent years. An example of this was the creation of MINAM in 2008 which, as stated in the recitals of the law that created it, was established within the framework of the delegation of powers granted to the Executive Power to facilitate the implementation of the Peru-USA TPA. MINAM was preceded by CONAM. that was created in 1994 as an entity attached to the Presidency of the Ministers Council.

VI.2.4 Competence of MINAM to regulate the INC in coordination with the Ministry of Economy and Finance

29. The Law of Sulfur Content in Diesel was enacted on March 22, 2006, that is, prior to the creation of MINAM (created by Legislative Decree No. 1013, dated May 14, 2008), which has an effect on the identification of the scope of said law from an institutional perspective.

30. Indeed, the Law of Sulfur Content in Diesel stated the following in relation to the definition of the competent authority to establish the INC:

> ***"Article 3.- Taxation measures to promote clean fuels***
> *The Selective Consumption Tax on fuels will be determined on a gradual basis, starting on January 1st, 2008, by introducing the criterion of proportionality into the degree of noxiousness that fuel pollutants have on the health of the population. To this end, the* ***Ministry of Economy and Finance, in coordination with the National Environmental Council (CONAM), will annually approve the indices of relative noxiousness that will be used.*** *This restructuring must be gradually carried out until January 1st, 2016, at the latest, when the taxation of fuels will fully consider the criterion of noxiousness."*
>
> (emphasis our own).

31. Although in 2007, MEF had issued a provision that established fixed amounts of the ISC considering the criterion of proportionality to the degree of noxiousness of fuels in accordance with the Law of Sulfur Content in Diesel (approved through Supreme Decree No. 211-2007-EF, which will be addressed below, see Section VI.C), MINAM has been the authority approving the regulations that established the INC in 2014, 2018 and 2020. It should be noted that each of the Supreme Decrees approved by MINAM on the matter had the endorsement of MEF.

32. Therefore, in the regulations issued by MINAM to approve the INC, it is mentioned that the Third Final Complementary Provision of Legislative Decree No. 1013, Law of Creation, Organization and Functions of the Ministry of the Environment, indicates that any reference made to CONAM, or the competencies, functions, and attributions that it had been exercising, shall be understood as carried out by MINAM.

33. Also, in said regulations it is indicated that according to sub-paragraph k) and n) of Article 7 of the Law of Creation of MINAM, this entity has among its specific functions those of promoting the protection of air quality and the development and use of technologies, practices and processes for clean production, selling and consumption. Likewise, it is indicated that sub-paragraph g) of Article 12 of the same law, indicates that the functions of the Vice Ministry of Environmental Management include, among others, those related to designing and approving the application of environmental prevention instruments related to the quality of the air, with the aim of guaranteeing optimum environmental quality.

34. Similarly, as part of the support of these Supreme Decrees issued by MINAM, reference is made to paragraph 10.2 of Article 10 of Law No. 28245, Framework Law of the National System of Environmental Management, which establishes that MINAM is empowered to dictate the provisions required to, among others, promote the use of clean

technologies and energy sources.

VI.3. Implementation of Article 3 of the Law of Sulfur Content in Diesel

VI.3.1. Intervention of the Ombudsman in relation to the implementation of the INC

35. The Ombudsman's Office (the Ombudsman) is a constitutionally autonomous body, whose functions include "defending the constitutional and fundamental rights of the person and the community, and to ensure the enforcement of the state administration duties, as well as the provision of public services to citizens."[14]

36. It should be noted that, in accordance with the provisions of the Organic Law of the Ombudsman's Office (Law 26520), the Ombudsman, as part of their investigations, may develop warnings, recommendations, reminders of legal duties, and suggestions for the adoption of new measures and present them to the public administration authorities, officials and servants. In all cases, the public authorities, public officials, and public servants are required to respond in writing within the non-extendable period of 30 days. If, as a result of the recommendations, an adequate measure is not adopted or the administrative entity does not inform the Ombudsman of the reasons for not adopting it, the latter may present background information of the matter and the recommendations to the Minister of the Sector or to the highest authority of the respective institution and, when appropriate, to the attention of the Office of the Comptroller General of the Republic[15].

37. In 2006[16], the Ombudsman, through Ombudsman Report No. 116, titled "Air Quality in Lima and its Impact on the Health and Life of its Inhabitants", stated that[17]:

> *"Taxation can be a powerful management tool, which has been clear in the Peruvian case with the Selective Consumption Tax (ISC) and the consumption of diesel, a fuel favored many years ago due to a lower tax burden that encouraged its widespread use for many years. As a direct result of the current structure of the ISC, most of the vehicles used for transport run on this fuel, which... is highly polluting due to its sulfur content... the production price of diesel was even higher than that of 97 octane gasoline. However, the price of gasoline ended up being four*

14 Political Constitution of Peru. 1993. Article 162.
15Law 26520. Organic Law of the Ombudsman's Office. Article 26.
16This Ombudsman Report does not have a specific publication date, only the year it was published.
17Ombudsman. Report No. 116, Air Quality in Lima and its Impact on the Health and Life of its Inhabitants, p.68.

soles higher than diesel due to the ISC, so while a gallon of diesel cost 1.7 Nuevos Soles, a gallon of 97 octane Gasoline cost 4.35 Nuevos Soles, that is, almost three Nuevos Soles more."

38. At the same time, the Ombudsman recognized the following in this report[18]:

"Esta situación, que incentivaba el consumo de un combustible que debía importarse y con alto contenido de azufre, ha comenzado a cambiar... En efecto, las diferencias en el monto del impuesto entre las gasolinas y el diésel se han reducido significativamente. Sin embargo, los precios al consumidor siguen favoreciendo el consumo del diésel."

39. It should be noted that the Ombudsman specifies that for this entity[19]:

"...what is important is not whether less polluting fuels pay taxes or not, but rather that the tax policy effectively considers the protection of the environment and people's health, so that there is a visible difference in taxation that encourages consumption towards fuels that cause fewer problems to health and the environment...Therefore, an important step forward is Law No. 28694, which regulates the sulfur content in diesel fuel, as it states that it is through taxation that the consumption of diesel fuel is guided in the medium term towards fuels that are less hazardous to health. The aforementioned law establishes that starting in 2008, the ***Ministry of Economy and Finance must set the amount of the ISC considering the index of noxiousness of the fuels that CONAM approves each year."***

(emphasis our own).

40. It is relevant to emphasize that the Ombudsman understands that under the scope of the Law of Sulfur Content in Diesel, MEF was responsible for setting the ISC considering the INC. This does not constitute interference in the powers of MEF as the governing body in the design of tax policy and in the issuance of tax regulations; however, according to what was indicated by the Ombudsman, such a function must be carried out within the scope of what is established in the Law under analysis. Likewise, it should be noted that this approach has been corroborated by the legal technical reports issued by MEF; as we point out in item VI.C.4.

18 Ibid. p.69.
19 Ibid. p.69.

41. In the aforementioned Ombudsman's Report, the Ombudsman's Office included the following recommendation regarding the INC:

"4. TO RECOMMEND the Ministry of Economy and Finance to incorporate environmental and health criteria when determining the Selective Tax on Fuel Consumption to encourage the use of less polluting fuels such as Liquefied Petroleum Gas and Natural Gas for Vehicles. In this regard, the application of the Index of Noxiousness of Fuels prepared by CONAM could be considered."

42. Subsequently, in August 2008, the Office of the Ombudsman issued Ombudsman Report No. 136, under the title "Air Quality in Lima and its Impact on the Health and Life of its Inhabitants: Follow-up of Ombudsman Recommendations".

43. In relation to the follow-up carried out on the aforementioned Recommendation, the Ombudsman notes the following:

"Through Official Letters No. 009-2007-DP/ASPMA and 287-2007-DP/ASPMA, dated March 23, 2007, and August 13, 2007, respectively, the Ombudsman requested information from MEF on the actions it had carried out for the implementation of the aforementioned recommendation.
*Through **Report No. 271-2007-EF/66.01, dated September 21, 2007, the General Directorate of Public Revenue Policy of MEF** informed us that, indeed, the ISC levies a lower amount of tax on the most polluting fuels; however, it agreed to consider other criteria, such as indices of noxiousness, for example, for the determination of the ISC. Therefore, said Directorate **indicated that the proposal would be evaluated for compliance with the provisions of Law No. 28694.***
Subsequently, in December 2007, Supreme Decree No. 211-2007-EF31 was approved, which approved the annual fixed amounts of the ISC applicable to fuels, considering the criterion of proportionality to the degree of noxiousness of fuels, for the 2008 – 2016 period."

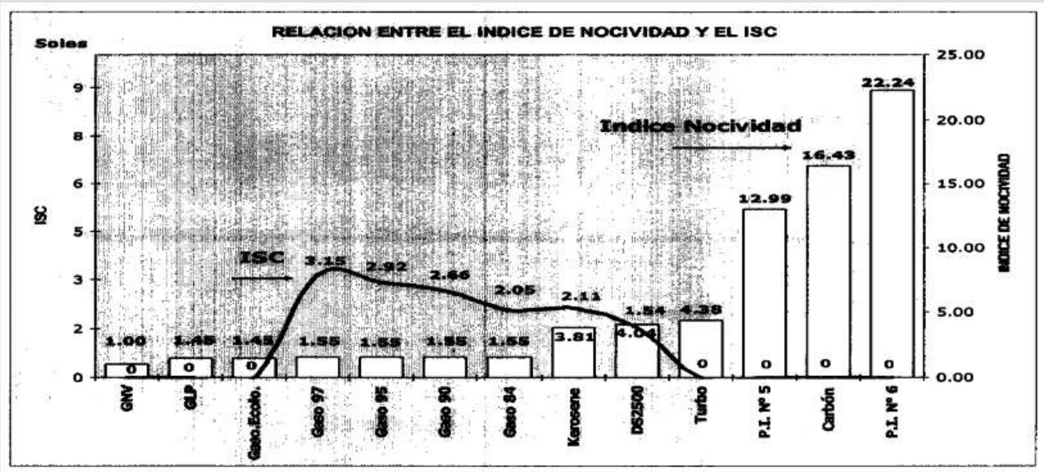
(emphasis our own).

44. In relation to the aforementioned Report No. 271-2007-EF/66.01, of September 2007, it notes the following:

3. It is necessary to point out some general considerations regarding the ISC that is currently levied on fuels derived from petroleum, such as:

- *A lower tax (fixed amount) is levied on the most polluting fuels (Diesel and Kerosene); while gasolines (less polluting fuels) are levied with higher taxes.*
- *Currently the ISC does not tax Natural Gas, Ecological Gasolines, Liquefied Petroleum Gas (LPG), Turbo Fuel, Industrial Oil and Coal or Coal.*
- *We agree that in the medium term the ISC matrix that taxes fuels must be changed, in such a way that the application of the Tax must consider the externality of fuels.*

4. The aforementioned can be summarized in the following graph where the current relationship between the noxiousness of fuels and the application of the ISC can be observed, from which the need to reverse the current tax matrix can be deduced:



Graphic: Relation between the INC and the ISC

45. This graph included in MEF Report No. 271-2007-EF/66.01 shows how the ISC was higher on less polluting fuels and, vice versa, lower on diesel, which is why the need to reverse this situation is acknowledged.

46. The Ombudsman warned that, in accordance with the provisions of Supreme Decree No. 211-2007-EM, "the introduction of the index of noxiousness, as well as the subsequent change in the determination of the ISC, will only take effect starting from the year 2009 for a specific group of fuels; while the index for other fuels, such as industrial oil and coal, would come into force starting in 2011. This is even though Law No. 28694 established that starting from January 2008 the criterion of noxiousness in the determination of the ISC be gradually applied." The following section develops in greater detail what this Supreme Decree notes.

47. In addition to making a reference to the date on which MEF would implement the application of the INC, the Ombudsman stated the following in relation to compliance with the Recommendation made on this matter[20]:

> *"…MEF has not complied with the recommendations made by the Ombudsman, since the fixed amounts approved are quite permissive, especially in the case of fuels such as industrial oil and coal whose levels of noxiousness exceed even those of diesel".*

48. Likewise, it is mentioned that:

> *"…in addition to being in breach of the defender's recommendation, MEF's action has been a transgression of the provisions of Law No. 28694. This constitutes a setback for Peruvian environmental management, particularly on air quality, and for the protection of the rights to health and life of the population, especially the most vulnerable people."*

49. Lastly, the Ombudsman notes the following in relation to the role of MEF in this matter:

> *"…MEF must seek formulas that allow the progressive incorporation of environmental and health criteria in the determination of the ISC, as prescribed by Law No. 28694, without this necessarily having a significant impact on the inflation rates. Likewise, environmental pollution causes distortions and failures in the markets, which can and should be prevented and corrected using economic instruments such as the ISC".*

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20 Ombudsman. Report No. 116, Air Quality in Lima and its Impact on the Health and Life of its Inhabitants: Follow up of Ombudsman Recommendations, p.51.

VI.3.2. Intervention of the Comptroller General of the Republic in relation to the implementation of the INC

50. The Office of the Comptroller General of the Republic (the Comptroller´s Office), which, like the Ombudsman's Office, is a constitutionally autonomous body, is responsible for supervising the legality of the Government Budget execution, of the operations of the public debt and of the acts of the institutions subject to control[21].

51. In 2011, the Comptroller's Office carried out a preventive control action in its oversight capacity, as part of the Annual Control Plan of the Department of Control of the Environment and Cultural Heritage, within the framework of Article 8 of Law No. 27785, Law of the National Control System and the Comptroller General of the Republic. The objective of this oversight action, carried out from December 15 to 22, 2011, was "to detect situations that generate risk in MINAM's management in relation to the promotion of the use of clean fuels through the updating of the INC within the framework of Law No. 28694, and issues related to air quality management[22].

52. As a result of this oversight action, the Comptroller's Office issued Report No. 659-2011-CG/MAC-VE4 called "Update of the Index of Noxiousness of Fuels and Issues Related to Air Quality Management", and identified the following as a risk:

> *"The lack of continuity of follow-up and coordination between the Ministry of the Environment and the Ministry of Economy and Finance leads to the risk that the index of noxiousness of fuels does not contribute to the effective promotion of the use of clean fuels."*

53. In this Report, the Comptroller's Office explicitly mentions Article 3 of the Law of Sulfur Content in Diesel, which regulates the sulfur content in diesel, as well as the Decree of the CONAM Directive Council that approved the INC for the 2005-2006 period. It also mentions Supreme Decree 211-2007-EF, which approved the Table of Fixed Amounts for Application of the ISC on fuels for the 2008-2016 period.

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21 Political Constitution of Peru. 1993. Article 82.
22 Comptroller General of the Republic. Report N° 659-2011-CG/MAC-VE. Update of the INC and issues related to air quality management. Oversight on the Ministry of the Environment. p.1.

54. In this regard, it is noted that MINAM had pointed out that during 2009 it had begun the process of updating the INC, carrying out inter-institutional coordination with the Ministries of Energy and Mines (MINEM) and MEF. As a result, in September 2009, MINAM sent the proposal of updated values of the INC to MEF, along with the bill of law for its respective approval. However, it is noted that MEF did not approve the aforementioned index despite the fact that MINAM made it a participant in this formulation process. More information on this subject is presented in item VI.C.3 b) of this document.

55. In particular, it is noted that[23]:

"MINAM did not continue with the coordination and monitoring of its proposal before MEF, in the 2010-2021 period, so the lack of approval of the INC would be limiting the determination of the Selective Tax on Fuel Consumption, and at the same time, said situation does not contribute to reducing air pollution levels in order to protect the health of the population in the country's urban centers. In this sense, the tax measures to promote cleaner fuels are not being fully applied in the country."

56. In turn, within the Recommendations of the aforementioned Report, the Comptroller noted the following action:

"2. Promote the approval and application of the Index of Noxiousness of Fuels as a tax measure to promote the use of cleaner fuels, in compliance with Law No. 28694."

57. It must be considered that this Comptroller's Report was prepared based on an oversight conducted in December 2011; this is more than five years after the approval of the Law of Sulfur Content in Diesel (of March 2006). As of that date, MINAM had not yet issued regulatory provisions on the INC.

23 Contraloría General de la República. Informe N° 659-2011-CG/MAC-VE. Actualización del Índice de Nocividad de Combustible y temas vinculados a la gestión de la calidad del aire". Veeduría al Ministerio del Ambiente. p.4

VI.3.3. Regulations developed to regulate the INC

a) Regulations under the scope of MEF

Supreme Decree No. 211-2007-EF

58. In December 2007, MEF approved Supreme Decree No. 211-2007-EF (December 23, 2007) establishing fixed amounts of the ISC considering the criterion of proportionality to the degree of noxiousness of fuels, in accordance with the provisions of the Law of Sulfur Content in Diesel.

59. This regulation refers to Article 3 of the Law of Sulfur Content in Diesel from its first recital, stating:

> *"That, for the purposes of complying with the provisions of Article 3 of the aforementioned Law, it is necessary to approve a schedule of the fixed amounts of the Selective Consumption Tax on fuels, determined based on the criterion of proportionality to the degree of noxiousness for the contaminants that they contain for the population, considering the aforementioned indices of noxiousness that may be progressively applied to said goods starting on January 1st, 2008."*

60. As can be seen, this regulation, approved in December 2007, was issued with the understanding that its application would start on January 1, 2008, which is the date that Article 3 of the Law of Sulfur Content in Diesel (of the year 2006) had established as the date from which the ISC for fuels should be determined with the introduction of the criterion of noxiousness.


CO2

61. In this context, the Supreme Decree No. 211-2007-EF approved the following table:

TABLE NO. 1: TABLE OF FIXED AMOUNT OF THE ISC ON FUELS DEFINED ACCORDING TO THE NOXIOUSNESS CRITERIA

Subpartidas Nacionales	Combustible	Monto Fijo del ISC (S/. por galón)								
		2008	2009	2010	2011	2012	2013	2014	2015	2016
2701.11.00.00/ 2701.19.00.00	Hulla (*)				70.00	80.00	90.00	100.00	110.00	120.00
	Gasolina para motores:									
2710.11.13.10 2710.11.19.00 2710.11.20.00	Con un Número de Octano Research (RON) inferior a 84	1.85	1.72	1.59	1.46	1.33	1.19	1.06	0.93	0.80
2710.11.13.20 2710.11.19.00 2710.11.20.00	Con un Número de Octano Research (RON) superior o igual a 84, pero inferior a 90	1.85	1.72	1.59	1.46	1.33	1.19	1.06	0.93	0.80
2710.11.13.30 2710.11.19.00 2710.11.20.00	Gasolina 90	2.46	2.25	2.05	1.84	1.63	1.42	1.22	1.01	0.80
2710.11.13.40 2710.11.19.00 2710.11.20.00	Gasolina 95	2.92	2.66	2.39	2.13	1.86	1.60	1.33	1.07	0.80
2710.11.13.50 2710.11.19.00 2710.11.20.00	Gasolina 97	3.15	2.86	2.56	2.27	1.98	1.68	1.39	1.09	0.80
2710.19.14.00	Queroseno.	1.94	1.94	1.93	1.93	1.92	1.92	1.91	1.91	1.90
2710.19.15.10/ 2710.19.15.90	Carburorreactores tipo queroseno para reactores y turbinas (Turbo A1)		0.26	0.53	0.79	1.05	1.31	1.58	1.84	2.10
2710.19.21.10/ 2710.19.21.90	Gasoils.	1.39	1.47	1.54	1.62	1.70	1.77	1.85	1.92	2.00
2710.19.22.10	Residual 6				0.52	1.03	1.55	2.07	2.58	3.10
2710.19.22.90	Los demás fueloils.				0.50	1.00	1.50	2.00	2.50	3.00
2711.12.00.00/ 2711.19.00.00	Gas Licuado de Petróleo (GLP)				0.08	0.17	0.25	0.33	0.42	0.50

(*) En este caso, será S/. por tonelada.

62. Likewise, the explanatory memorandum of this norm states that the purpose of this norm was to comply, in particular, with Article 3 of the Law of Sulfur Content in Diesel, indicating the following:

> *"I. Background-.*
> *Article 3 of Law No. 28694 establishes that the Selective Consumption Tax on Fuels will be determined on a gradual basis, starting on January 1st, 2008, by introducing the criterion of proportionality into the degree of noxiousness that the fuel pollutants have on the health of the population.*
> *The aforementioned law adds that this restructuring of the ISC applicable to fuels must be gradually carried out until January 1st, 2016, at the latest, when the said taxation of fuels will fully consider the criterion of noxiousness.*
> *In this sense,* ***with the aim to comply with the provisions of Article 3 of the aforementioned law, it is necessary to approve a table of the fixed amounts of the ISC for fuels, determined based on the criterion of proportionality to the degree of noxiousness that fuel pollutants have on the health of the population, taking into account the indices of noxiousness approved by the Board of Directors of the National Environmental Commission*** *(sic)* ***(CONAM)***

for the 2005-2006 period, which may be gradually applied to said goods starting on January 1st, 2008.
This Supreme Decree notes the table of the fixed amounts of the ISC for fuels that may be gradually applied to the aforementioned goods starting on January 1st of each year... ***compliance with the provisions of the aforementioned table will allow for the fixed amount of the ISC applicable to each of the fuels to be completely determined based on their indices of noxiousness in 2016."***

(emphasis our own).

63. In turn, in relation to the cost-benefit analysis, item III of the explanatory memorandum of this law states that (air) pollutants generate negative effects on society, which end up being assumed by the Government as social spending, as this law was intended for the most polluting fuels to bear a higher tax burden, which would contribute to reducing this type of social spending.

64. It should be noted that the legal formula of this law indicates a programmatic (or referential) nature of its application under the following text:

Article 1.- ***APPROVAL OF THE TABLE OF FIXED AMOUNTS OF THE ISC ON FUELS***
May the table of the fixed amounts of the Selective Consumption Tax applicable to fuel be approved. The fixed amounts are determined based on the criterion of noxiousness, which is detailed in the Annex that is part of this Supreme Decree, ***the same amounts that may be set for said goods gradually from January 1st of each year.***

(emphasis our own).

65. It must be considered that in the aforementioned Ombudsman Report No. 136 (2008), the Ombudsman's Office pronounces on the scope of Supreme Decree No. 211-2007-EF, indicating that under its scope, the application of the fixed amounts of the ISC that this norm regulated would be applicable under MEF's discretion taking into account the aforementioned wording of Article 1 of this law.

66. In the Ombudsman's opinion, this wording could give rise to interpretations that do not necessarily consider the criteria for protecting the environment and the health of the population. It is even mentioned that this would have been MEF's interpretation by having replaced, in March and June 2008, Appendix III of the TUO of the Law on IGV and ISC, having established that the amount of the ISC of diesel fuels, maintained a downward trend , "without taking into account the provisions of Law No. 28694, which establishes the consideration of the index of noxiousness of fuels for the determination of the ISC"[25].

67. The Ombudsman even notes the following, in relation to this Supreme Decree No. 211-2007-EF[26]:

> *"The approval of said Supreme Decree was a mere formality given that today, the provisions of Annex III of the Single Ordered Text of the Law on General Sales Tax and Selective Consumption Tax are applied, which do not take into account the criteria of noxiousness to define the amount of the ISC."*

68. Likewise, among the conclusions of said Ombudsman Report No. 136, the Ombudsman noted that[27]:

> *"Although MEF issued Supreme Decree No. 211-2007-EF, which inserted the criterion of proportionality into the degree of noxiousness of fuels, the criterion has not been applied. Currently, the modification of Appendix III of the Single Ordered Text of the Law on General Sales Tax and Selective Consumption Tax prevails, which maintains and consolidates the tendency to reduce the ISC, without considering the criterion of protection of the environment and the health of the population."*

69. An additional aspect of Ombudsman Report No. 136 mentions that the regulations on the ISC should have been approved, within the framework of the Law of Sulfur Content in Diesel, in coordination with the national environmental authority, which was at the time CONAM, noting that[28]:

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24 Reference is made to Supreme Decrees No. 037-2008-EF and 071-2008-EF, published in the Official Gazette El Peruano, on March 7 and June 1, 2008, respectively, which replaced the new Appendix III of the TUO of the Law on General Sales Tax and Selective Consumption Tax, approved by Supreme Decree No. 055-99-EF.
25 Ombudsman. Report No. 116, Air Quality in Lima and its Impact on the Health and Life of its Inhabitants: Follow up of Ombudsman Recommendations, p.53.
26 Ibid.
27 Ombudsman. Report No. 116, Air Quality in Lima and its Impact on the Health and Life of its Inhabitants: Follow up of Ombudsman Recommendations, p.115.

"to date, only the index of noxiousness of fuels has been approved for the 2005-2006 period, which is why MEF had to consider said index to determine the amounts of the ISC up 2016. However, what would be most appropriate is to annually modify the norm that approves the amounts of the ISC with the aim of adjusting these amounts to the indices of noxiousness approved each year."

70. In relation to the scope of this law, Castro (2010) pointed out that, through this law:

"A fixed amount of the Selective Consumption Tax is approved for the various types of fuel until 2016, introducing, by all appearances, the criterion of a higher amount of the tax on the most polluting fuels. … This Law also established that the Ministry of Economy and Finance, in coordination with the National Environmental Council, will annually approve the relative indies of noxiousness that will be used until 2016 at the latest, the date on which the tax levied fuels will fully consider the criterion of noxiousness'"[29].

(author's emphasis)

71. Likewise, Castro (2010) notes that:

"MEF, without having the Index of Noxiousness of Fuels for 2007 or for 2008, has forecasted the amount of the ISC that will be applied to the sale of fuels until 2016. How can MEF predict the quality that the fuels will have during each of the next eight years? Why does MEF not take advantage of a tax instrument, nor of a platform of coordination with the national environmental authority, to encourage the improvement of fuel quality in Peru?[30]*"*.

72. It should also be noted that after the approval of this regulation (Supreme Decree 211-2007-EF, of December 23, 2007), three legal norms were issued modifying Annex III of this Supreme Decree.

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28 Ombudsman. Report No. 116, Air Quality in Lima and its Impact on the Health and Life of its Inhabitants: Follow up of Ombudsman Recommendations, p.51.
29 Castro, M. (2010). "The integration of health and the environment in public policies: Avoiding air pollution". Scientific Magazine 7(2). Universidad Científica del Sur. p.144.
30 Ibid.

73. These norms were the following:

CHART NO.2:
NORMS THAT MODIFY THE ANNEX III OF SUPREME DECREE NO.055-99-EF THAT REGULATES THE ISC ON FUELS THAT MENTION SUPREME DECREE NO. 211-2007-EF

DATE	LEGAL REGULATION	MENTIONS OF SUPREME DECREE 211-2007-EF
October 29, 2008	Supreme Decree No. 126-2008-EF	- The amounts of Kerosene and Diesel 2 are increased so that their fixed amounts come close to the level proposed for 2009 in Supreme Decree 211-2007-EF "progressively complying with the scheme of introducing the criterion of noxiousness in the aforementioned tax". - The tax on residual fuels is applied earlier, which according to Supreme Decree 211-2007-EF was scheduled for 2011.
November 15, 2008	Supreme Decree No. 131-2008-EF	- This norm will allow 84 and 90 octane gasoline to rectify their respective fixed amounts so that they would not be below the goal set for 2016 by Supreme Decree 211-2007-EF. - In the case of Kerosene and Diesel 2, it would be possible that the increase in their respective fixed amounts be those foreseen for 2009, reducing the lag related to what is stipulated in Supreme Decree211-2007-EF.
December 24, 2010	Supreme Decree No. 265-2010-EF	- This norm mentions the following: “In order to comply with Law No. 28694, through Supreme Decree No. 211-2007-EF, a table of fixed amounts of the ISC applicable to fuels was approved, determined on the basis of the index of noxiousness of fuels, which must be applied gradually from 2008 to 2016”.

b) Regulations under the scope of MINAM

74. This section presents both the documentation related to the process of approving regulations for the implementation of Article 3 of the Law of Sulfur Content in Diesel (even when these have not been approved), as well as the regulations issued by MINAM for the implementation of said article.

FACTUAL RECORD

Draft regulation: 2008 - 2009

75. The reference to a first communication, dated August 1, 2008, via email, sent by the Vice Ministry of Environmental Management to the Vice Ministry of Economy in relation to the regulation of INC, has been identified. The reference to this communication can be found in the following document:

PERÚ | Ministerio de Economía y Finanzas | Viceministro de Economía

000020

"DECENIO DE LAS PERSONAS CON DISCAPACIDAD EN EL PERÚ"
"AÑO DE LAS CUMBRES MUNDIALES EN EL PERÚ"

Lima, 22 OCT. 2008

MINISTERIO DEL AMBIENTE
RECIBIDO
21 OCT. 2008
MINISTERIO DEL AMBIENTE
003374

OFICIO Nº 286 -2008-EF/15

Señora
ANA MARÍA GONZALEZ DEL VALLE B.
Vice Ministra de Gestión Ambiental
Ministerio del Ambiente
Presente.-

Referencia : *Correo Electrónico de fecha 01-08-2008*

Por medio del presente es grato dirigirme a usted en relación al documento de la referencia, mediante el cual remite el proyecto de Decreto Supremo de aprobación de los Índices de Nocividad de los Combustibles (INC).

Al respecto, informamos que dicha documentación no incluye la guía metodológica de actualización de los referidos INC. Asimismo, se observa en el proyecto importantes cambios con relación a los INC aprobados por el CONAM para el periodo 2005-2006 (actualmente vigentes). En razón a ello, solicitamos se remita la exposición de motivos y la guía metodológica correspondiente, explicando las razones de dichas variaciones, debido a que los nuevos INC tendrían implicancias en la determinación del Impuesto Selectivo al Consumo (en virtud de la Ley Nº 28694, Ley que regula el contenido de azufre en el combustible diesel), a aplicarse progresivamente a partir del año 2008.

Es propicia la ocasión para reiterarle mi consideración distinguida.

Atentamente,

EDUARDO A. MORÓN PASTOR
Viceministro de Economía

MINISTERIO DEL AMBIENTE
VICE-MINISTERIO DE GESTIÓN AMBIENTAL
RECIBIDO
22 OCT. 2008
Vº Bº ________ Hora: ________
Firma ________

Jr. Junin Nº 319, Lima – Teléfonos 3119900 3115930

(101028)

Lima, October 22, 2008
Official Letter No. 286-2008-EF/15
Mrs.
Ana María Gonzalez del Valle B.
Vice Minister of Environmental Management
Ministry of the Environment

Reference: Email dated August 1, 2008

I am hereby pleased to address you in relation to the referenced document, through which you submit the draft Supreme Decree approving the Fuel Noxiousness Indices (INC).

In this regard, we inform that said documentation does not include the methodological guide for updating the aforementioned INC. Likewise, important changes are observed in the project in relation to the INC approved by CONAM for the 2005-2006 period (currently in force). Due to this, we request that you send the explanatory memorandum and the corresponding methodological guide, explaining the reasons for said variations, because the new INC would have implications in the determination of the Selective Consumption Tax (by virtue of Law No. 28694, Law of Sulfur Content in Diesel), to be applied gradually starting in 2008.

This is an opportune occasion to reiterate my distinguished consideration.

Sincerely,
Eduardo A. Moron Pastor
Vice Minister of Economy

[Received October 22, 2008]

76. As can be seen, on August 1st, 2008, the Vice Ministry of Environmental Management had sent, by email, a draft Supreme Decree approving the INC to the Vice Ministry of Economy.

77. In response to said submission, the Vice Ministry of Economy dated October 21, 2008, sent Official Letter No. 286-2008-EF/15 requesting the Vice Ministry of Environmental Management to send the methodological guide and explanatory memorandum for the regulatory draft. It should be noted that, in this communication, MEF indicates that the new INC would have implications in the determination of the ISC starting in 2008.

78. In turn, on January 9, 2009, through Official Letter No. 006-2009-EF/15.01, the Vice Ministry of Economy addresses the Vice Ministry of Environmental Management urgently requesting the definition of the INC for biofuels within the framework of specific regulations on this matter:

PERÚ | Ministerio de Economía y Finanzas | Viceministro de Economía

000219

"DECENIO DE LAS PERSONAS CON DISCAPACIDAD EN EL PERÚ"
"AÑO DE LA UNIÓN NACIONAL FRENTE A LA CRISIS EXTERNA"

RECIBIDO
12 ENE. 2009
MINISTERIO DEL AMBIENTE

Lima, 09 ENE. 2009

OFICIO N° 006 -2009-EF/15.01

Señora
ANA MARÍA GONZÁLEZ DEL VALLE BEGAZO
Viceministra de Gestión Ambiental
Ministerio del Ambiente
Av. Guardia Civil 205 - Lima 41
Presente.-

DESPACHO MINISTERIAL
RECIBIDO
12 ENE. 2009
V° B° ________ Hora: ________
Firma ________
5234

Asunto : *Información sobre los índices de nocividad de los productos: Biodiesel B100, Diesel B2, Diesel B5 y Diesel B20.*

Tengo el agrado de dirigirme a usted, a fin de solicitarle se sirva informar los índices y/o grado de nocividad del Biodiesel B100, así como de los Diesel BX (B2, B5, B20), información que se requiere con carácter de urgente, habida cuenta que de acuerdo a lo establecido por la Ley N° 28054 y sus normas reglamentarias[1], a partir del 01 de enero de 2009, las refinerías sólo comercializarán Diesel B2, el cual se obtiene de una mezcla de Diesel N° 2 (98%) y del Biodiesel B100 (2%).

Cabe mencionar que esta información resulta indispensable para evaluar la aplicación del Impuesto Selectivo al Consumo a cada uno de dichos bienes en función a su grado de nocividad, de conformidad con lo dispuesto en el artículo 3° de la Ley N° 28694, Ley que regula el contenido de azufre en el combustible diesel.

Sin otro particular, aprovecho la oportunidad para expresarle los sentimientos de mi especial consideración.

Atentamente,

MINISTERIO DEL AMBIENTE
VICE-MINISTERIO DE GESTIÓN AMBIENTAL
RECIBIDO
13 ENE. 2009
V°B° ________ Hora: 12:20
Firma ________

EDUARDO A. MORÓN PASTOR
Viceministro de Economía

[1] *Decretos Supremos N°s 021-2007-EM y 064-2008-EM.*

Jr. Junín N° 319 Lima 1 - Teléfonos 311-9900 311-5930

(002832)

(The document was received containing these highlights.)

Lima,
OFFICIAL LETTER No. 006-2009-EF/15.01
Mrs.
ANA MARIA GONZALEZ DEL VALLEY B.
Vice Minister of Environmental Management
Ministry of the Environment
Av. Guardia Civil 205 - Lima 41

Subject: Information on the indices of noxiousness of the products: Biodiesel B100, Diesel B2, Diesel B5 and Diesel B20.

I have the pleasure of writing to you to request that you provide information about the indices and/or degree of noxiousness of Biodiesel B100, as well as Diesel BX (B2, B5, B20), which is urgently required, taking into account that according to the provisions of Law No. 28054 and its regulations (1), as of January 1, 2009, refineries will only market Diesel B2, which is obtained from a mixture of Diesel No.2 (98%) and Biodiesel B100 (2%).

It is worth mentioning that this information is essential to evaluate the application of the Selective Consumption Tax to each of said goods based on their degree of noxiousness, in accordance with the provisions of Article 3 of Law No. 28694, Law of Sulfur Content in Diesel.

Without any further issue to discuss, I take the opportunity to express the sentiments of my special consideration.

Sincerely,

Eduardo A. Moron Pastor
Vice Minister of Economy
[Received January 13, 2009]

(The document was received containing these highlights)

79. In this second communication, MEF notes that the information on the indices of noxiousness of fuels is essential to evaluate the application of the ISC, in accordance with the provisions of Article 3 of the Law of Sulfur Content in Fuel.

80. In response to these two communications, the Vice Ministry of Environmental Management forwarded Official Letter No. 0056-2009-DVMGA/MINAM dated January 27, 2009, to the Vice Ministry of Economy as shown below

"Año de la Unión Nacional Frente a la Crisis Externa"
"Decenio de las Personas con Discapacidad en el Perú"

CARGO

PERÚ | Ministerio del Ambiente | Viceministerio de Gestión Ambiental

000001

Lima, 27 de Enero de 2009

OFICIO N° 0056 -2009-DVMGAM/MINAM

MINISTERIO DEL AMBIENTE
RECEPCION
30 ENE. 2009
RECIBIDO
Firma: .... Hora: ....

Doctor
JOSE BERLEY ARISTA ARBILDO
Viceministro de Economía (e)
MINISTERIO DE ECONOMÍA Y FINANZAS
Jr. Junín Nº 319
Lima.-

Asunto: Índices de Nocividad de Combustible
Referencia: 1. Oficio Nº 286 – 2008-EF/15
2. Oficio Nº 006 – 2009-EF/15.01

De mi mayor consideración:

Es grato dirigirme a usted para saludarle atentamente y a la vez dar atención a la solicitud realizada mediante los documentos de la referencia, sobre los valores propuestos de Índices de Nocividad de Combustibles para su aplicación al Impuesto Selectivo al Consumo, de acuerdo a lo establecido mediante la Ley Nº 28694, que regula el Contenido de Azufre de los combustibles y establece que en forma coordinada el MEF y el MINAM procederán a la aprobación de los Índices de Nocividad.

En tal sentido, mediante el presente hago llegar el informe técnico correspondiente al desarrollo del estudio, en el cual se explica los motivos de variación de los valores propuestos; así mismo se adjunta el Informe Final de la consultora encargada del Estudio para elaboración de la Guía Metodológica; por otra parte en un segundo anexo se incluye la exposición de motivos solicitada.

Sin otro particular por el momento, aprovecho la ocasión para expresar los sentimientos de mi especial consideración y estima.

Atentamente,

MINISTERIO DEL AMBIENTE – VICEMINISTERIO GESTIÓN AMBIENTAL – MINAM

Ana María González del Valle
VICEMINISTRA DE GESTIÓN AMBIENTAL
Ministerio del Ambiente

AMGVB/rlmo
Cc. Archivo

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COMPAÑIA/CO.	MEF	COMPAÑIA/CO.	MINAM
DEPARTAMENTO/DEPT.		TELEFONO/PHONE #	
FAX	4280314	FAX	2251202

Lima, January 27, 2009
Official Letter No. 0056-2009-DVMGAM/MINAM
Doctor
Jose Berley Arista Arbildo
Viceministro de Economía
Ministerio de Economía y Finanzas
Jr. Junín No. 319
Lima.-

Subject: Indices of Noxiousness of Fuels
Reference: 1. Official Letter No. 286-2008-EF/15
2. Official Letter No. 006-2009-EF/15.01

Of my highest consideration:

It is a pleasure to address you to respectfully greet you and at the same time pay heed to the request made through the referred documents about the proposed values of Indices of Noxiousness of Fuels for their application to the Selective Consumption Tax, in accordance with what is established by means of the Law No. 28694, which regulates the Sulfur Content of fuels and establishes that MEF and MINAM will proceed to approve the Indices of Noxiousness in a coordinated manner.

Therefore, I hereby send the technical report corresponding to the development of the study, in which the reasons for the variation of the proposed values are explained: likewise, the Final Report of the consultant in charge of the Study for the elaboration of the Methodological Guide is attached. Additionally, a second annex includes the explanatory memorandum requested.

Without any further issue to discuss, I take advantage of the occasion to express the sentiments of my special consideration and esteem.

Sincerely,

Ana María González del Valle
Vice Minister of Environmental Management
Ministry of the Environment

81. Based on the documents presented above, we can verify that in the years 2008-2009, MINAM and MEF coordinated for the approval of the INC, but it was not until 2014 that MINAM approved the first INC, as indicated below:

Index of Noxiousness of Fuels 2014-2015

82. Through Supreme Decree 006-2014-MINAM, of May 1, 2014, the Indices of Noxiousness (INC) was approved for the 2014-2015 period.

83. In relation to the temporality of this regulation, the explanatory memorandum states the following:

> ***"I. GROUNDS***
> *...The Index of Noxiousness of Fuels 2014-2015 has been the subject of consultation and has been developed with the basic information on emission factors and weighting according to human toxicity available in the literature or existing methodologies to date. Therefore, it is expected that this index must evolve and* ***must be updated annually as information that is new or in greater detail is generated,*** *specifically in relation to the emission factors according to categories and pollutants. Therefore, it is through the Decree of the Directive Council No. 018-2005-CONAM- CD, the Index of Noxiousness of Fuels for the 2005-2006 period was approved,* ***which is why it is necessary to bring said values up to date."***
>
> (emphasis our own).

Index of Noxiousness of Fuels 2018-2019

84. By Supreme Decree No. 003-2018-MINAM, of May 9, 2018, the INC was approved for the 2018-2019 period.

85. In relation to the temporality of this regulation, the following documents should be noted:

- *Report issued by the General Office of Legal Counsel of MINAM (Report No. 185-2018-MINAM/SG/OGAJ) dated March 8, 2018, in relation to the draft Supreme Decree that would approve the INC for the 2018-2019 period, which indicates the following*

  "II. ANALYSIS:

  2.10 For this reason, through Supreme Decree No. 006-2014-MINAM, endorsed by the ministers of the environment and economy and finance, the Index of Noxiousness of Fuels (INC) was approved for the 2014-2015 period.

  2.11 Considering that said period has ended, the Directorate of Environmental Quality and Eco-efficiency of the General Directorate of Environmental Quality, *through Report No. 0050-2018-MINAM/VMGA/DGCA/DCAE,* ***proposes the regulatory project that approves the Index of Noxiousness of Fuels (INC) for the 2018-2019 period and its corresponding*** *explanatory memorandum..."*

  (emphasis our own).

- *The explanatory memorandum of this regulation states the following:*

  "I. Analysis of the legality and constitutionality of the draft supreme decree
  (...)

  Precisely, under this regulatory context, the Indices of Noxiousness of Fuels (INC) were approved for the 2014-2015 period by Supreme Decree No. 006-2014-MINAM, endorsed by the Ministers of the Environment and Economy and Finance.
  However, ***to date, the approval of the update of the Fuel Noxiousness Indices for the 2018-2019 period is necessary, considering the current characteristics of the energy matrix in the country.***
  Accordingly, MINAM, in coordination with MEF, has prepared the draft Supreme Decree that approves the updating of the Indices of Noxiousness of Fuels for the 2018-2019 period, and repeals Supreme Decree No. 006-2014-MlNAM.
  In this regard, it should be noted that ***this proposed regulation has been prepared considering the current characteristics of the energy matrix in the country,*** *as well as the Government's objective of carrying out sustainable development and maintaining a clear legal framework."*

  (emphasis our own).

Index of Noxiousness of Fuels 2020-2021:

86. The Supreme Decree N°007-2020-MINAM, of August 18, 2020, approved the INC for the 2020-2021 period.

87. In relation to the temporality of this regulation, its explanatory memorandum mentions the following:

> *"…according to Article 3 of Law No. 28694, MINAM, in coordination with MEF, has prepared the present draft Supreme Decree,* ***considering the need to approve the Fuel Noxiousness Indices for the 2020-2021 period.***
> *In this regard, it should be noted that* ***this draft regulation has been prepared considering the current characteristics of the energy matrix in the country****, as well as the Government´s objective of carrying out sustainable development and maintaining a clear legal framework."*
>
> (emphasis our own).

88. Taking into account the reference done to the current energy matrix of the country, it should be noted that MINEM, through its General Directorate for Energy Efficiency, each year publishes a National Energy Balance that contains the results of the physical flows of the different energy sources used in the country, including the national energy matrix. The last balance approved was for 2019 and published in 2021.

89. It should be noted that, although MINAM, in coordination with MEF, has been approving the aforementioned INC, the Law of Sulfur Content in Diesel had indicated that gradually, from January 1, 2008, to January 1, 2016, the taxation of fuels must fully consider the criterion of noxiousness. However, MINAM has in fact continued to issue Supreme Decrees after 2016 (in 2018 and 2020) approving these INC, and it is likely that this will continue in the future. The INC approved by MINAM are not reflected in the ISC approved by MEF (see item VI.3.4.).

VI.3.4. Regulations developed by MEF to regulate the ISC and its relationship with the INC

90. The TUO of the Law on the General Sales Tax and ISC approved by Supreme Decree No. 055-99-EF, establishes the authority of MEF to regulate the application of the IGV on fuel, by noting the following

> ***"Article 61.- MODIFICATION OF RATES AND/OR FIXED AMOUNTS***
> *By Supreme Decree endorsed by the Minister of Economy and Finance, the rates and/or fixed amounts may be modified, as well as the goods contained in Appendices III and/or IV.*
> *To this end, the modification of Appendix III goods can only include fossil and non-fossil fuels, mineral oils and products of their distillation, bituminous materials, and mineral waxes…"*

91. From this date on, a series of regulations have been issued that modified Annex III (now called "New Annex III), which is the one that regulates the IGV on fuels.

92. It should be noted that the development of this tax regulation is formulated within the framework of the Tax Policy Guidelines of the Multiannual Macroeconomic Framework periodically approved by the Ministers Council.

93. Below is a detailed list of the regulations that have been modifying the fixed amounts of the ISC for fuels, from its original regulation to the present date. At the same time, it includes, in parallel, the issuance of the INC approved by MINAM:

CHART NO. 3:
NORMATIVE EVOLUTION OF THE ISC ON FUELS AND ITS RELATION WITH THE NORMS ISSUED BY MINAM ABOUT INC

	DATE (the dates follow the European / Latin American format: Day/Month/-Year)	REGULATION OF ANNEX III OF UNIQUE ORDERED TEXT (TUO) OF THE GENERAL SALES TAX - ISC (Supreme Decree No. 055-99-EF and modifications)	REASONS FOR THE MODIFICATION TO THE ISC FROM THE APPROVAL OF THE LAW OF SULFUR CONTENT IN DIESEL (MARCH 22, 2006)	MINAM/CONAM LEGAL REGULATION REGARDING THE INC
1	23.04.1996	Legislative Decree No. 821		
2	12.03.1997	Supreme Decree No. 025-97-EF		
3	12.08.1997	Supreme Decree No. 108-97-EF		
4	12.01.1998	Supreme Decree No. 002-98-EF		
5	24.03.1998	Ministerial Resolution No. 062-98-EF-15		
6	08.07.1998	Ministerial Resolution No. 157-98-EF/15		
7	06.04.1999	Supreme Decree No. 045-99-EF		
8	22.12.2000	Supreme Decree No. 142-2000-EF		
9	24.03.2001	Supreme Decree No. 049-2001-EF		
10	07.04.2001	Ministerial Resolution No. 115-2001-EF-15		
11	02.08.2005	Supreme Decree No. 099-2005-EF		
12	10.09.2005	Supreme Decree No. 115-2005-EF		
A	02.12.2005			Decree of the Directive Council No. 018-2005-CONAM-CD. INC for the 2005-2006 period
13	31.12.2005	Supreme Decree No. 194-2005-EF		
14	13.04.2006	Supreme Decree No. 044-2006-EF	Increase in the international price for petroleum	
15	25.04.2006	Supreme Decree No. 051-2006-EF	Increase in the international price for petroleum	
16	15.08.2006	Supreme Decree No. 135-2006-EF	Increase in the international price for petroleum	
17	21.05.2007	Supreme Decree No. 060-2007-EF	New customs tariff	
18	02.09.2007	Supreme Decree No. 135-2007-EF	Adjustment in ISC for aviation fuel	

FACTUAL RECORD

CHART NO. 3:
NORMATIVE EVOLUTION OF THE ISC ON FUELS AND ITS RELATION WITH THE NORMS ISSUED BY MINAM ABOUT INC

19	23.12.2007	Supreme Decree No. 212-2007-EF	Increase in the international price for petroleum	
20	07.03.2008	Supreme Decree No. 037-2008-EF	Increase in the international price for petroleum	
21	01.06.2008	Supreme Decree No. 071-2008-EF	Increase in the international price for petroleum	
22	29.10.2008	Supreme Decree No. 126-2008-EF	Compliance to Supreme Decree No. 211-2007-ef	
23	15.11.2008	Supreme Decree No. 131-2008-EF	Cumplimiento Decreto Supremo No.211-2007-EF	
24	04.03.2009	Supreme Decree No. 054-2009-EF	Art.3 of Law 28694	
25	31.12.2009	Supreme Decree No. 322-2009-EF	Art.3 of Law 28694	
26	22.01.2010	Supreme Decree No. 013-2010-EF	Art.3 of Law 28694	
27	24.12.2010	Supreme Decree No. 265-2010-EF	Art.3 of Law 28694	
28	29.12.2010	Supreme Decree No. 270-2010-EF	Art.3 of Law 28694	
29	08.06.2011	Supreme Decree No. 097-2011-EF	Increase in the international price for petroleum	
B	01.05.2014			Supreme Decree No. 006-2014-MINAM INC for the 2014-2015 period
30	21.11.2014	Supreme Decree No. 316-2014-EF	INC 2014-2015-MINAM	
31	05.05.2016	Supreme Decree No. 111-2016-EF	INC 2014-2015-MINAM	
32	11.11.2016	Supreme Decree No. 306-2016-EF	INC 2014-1016-MINAM	
33/C	09.05.2018	Supreme Decree No. 094-2018-EF	INC sent by MINAM via email	Supreme Decree No. 003-2018-MINAM INC for the 2018-2019 period
D	18.08.2020			Supreme Decree No. 007-2020-MINAM INC for the 2020-2021 period
34	03.04.2022	Supreme Decree No. 068-2022-EF	Temporary exclusion (until June 30, 2022) of a group of fuels due to international prices of imported fuels and foods	

94. The above table shows that the norms that regulate the ISC on fuels, which were approved in 1996 (Legislative Decree No. 821), have been subject to 33 modifications by MEF to date in the exercise of the competence attributed to it.

95. Of this set of modifications, it should be noted that after the Law of Sulfur Content in Diesel (March 22, 2006) was enacted, eight modifications of the ISC on fuels were approved, none of which were related to the application of the INC but rather to the increase in the price of fuels or for tariff identification. It was not until 10 months after the approval of Supreme Decree No. 211-2007-EF (December 23, 2007, the regulation that established the table of fixed amounts of the ISC for fuels considering the criterion of noxiousness), that the Law of Sulfur Content in Diesel started to be referenced in modifications to the ISC (by Supreme Decree No.126-2008-EF of October 29, 2008).

96. Indeed, of the total of 13 modifications from the aforementioned Supreme Decree No. 126-2008-EF, only two have been based on aspects related to the prices of fuel and other goods (as is the case of the price of food, in the regulation issued in 2022). Therefore, most of the modifications issued after the issuance of Supreme Decree No. 211-2007- EF have had the progressive implementation of the noxiousness criterion in the ISC for fuels by MEF as its main objective.

97. Now, to have a comprehensive look, we must consider how the approval of the INC by MINAM (with the endorsement of MEF) has impacted the ISC regulation of fuels.

98. In this regard, first of all, it should be noted that, as the Government of Peru has pointed out that "the INC serves as a scale of reference for the Ministry of Economy and Finance to establish criteria of proportionality in the distribution of the ISC of fuels" (Technical Report No. 801-2013-DGCA-VMGA/MINAM). At the same time, it should be remembered that as stated in Article 36 of the LGA, Law No. 28611, in the exercise of their respective functions, public entities incorporate economic instruments, including taxes, to encourage environmentally appropriate practices and compliance with the objectives of the National Environmental Policy and environmental standards.

99. First, both regulatory instruments (the INC and the ISC) are prepared based on a categorization of fuels that is not standardized, or that, in any case, are categories that vary across time. Said standardization could be achieved with the participation of MINEM as the competent authority in the matter.

100. Reviewing the first modification to the ISC after the approval of the first INC by MINAM (2014-2015 period), the following can be identified:

- The explanatory memorandum of this regulation (Supreme Decree No. 316-2014-EF) explicitly mentions the regulation approved by the INC for the 2014-2015 period (Supreme Decree No. 004-2014-MINAM), noting that "Although the INC does not establish values directly related to the amount of the ISC, it does allow these ratios to be taken as a scale of reference so that proportionality criteria are established in the distribution of the ISC of fuels". At the same time, it is pointed out that given the decrease in the international price of oil, it is necessary to reduce the ISC in less polluting fuels, such as gasoline and gasohols.

- We will have the following result when integrating both regulations:

CHART NO.4:
RELATION BETWEEN THE INC 2014-2015 AND THE APPENDIX III OF THE TUO OF THE IGV-ISC

FUEL	INC 2014-2015 SUPREME DECREE 006-2014-MINAM (May 1, 2014)	MODIFICATION TO ANNEX OF TUO ISC: SUPREME DECREE 316-2014-EF (November 21, 2014)
GASOHOL 84	1.45	S/ 0.88
GASOHOL 90	1.31	S/ 0.99
GASOHOL 95	1.31	S/ 1.07
GASOHOL 97	1.31	S/.1.13

Although, on the one hand, the INC is expressed in digits and the ISC is expressed in amounts of money, we can point out that, in order for the ISC to be consistent with the INC's regulatory approach, and to respect the criteria of proportionality that the INC establishes, the amount of the tax on 84-octane gasohol should be greater than the one corresponding to gasolines with a higher octane number, which are cleaner; however, as seen above, this is not the case. Indeed, the ISC amount that was indicated for 84-octane gasohol was S/.0.88, while the ISC amount for 97-octane gasohol was S/.1.13.

101. In the case of the second INC approved by MINAM (2018-2019 period):

CHART NO.5:
RELATION BETWEEN THE INC 2018-2019 AND THE APPENDIX III OF THE TUO OF THE IGV-ISC

FUEL	INC 2018-2019 SUPREME DECREE 003-2018-MINAM (May 9, 2018)	MODIFICATION TO III: SUPREME DECREE 094-2018-EF (May 9, 2018)
GASOHOL 84	1.45	S/ 0.88
GASOHOL 90,95,97	5.2	S/. 1.13

Although both regulations were approved on the same day in this case, it is relevant to note that under the logic of the INC approved by MINAM, the ISC value of 84-octane gasoline (30.8) has a value six times higher (600%) than that of the other gasolines (5.2); however, as it can be seen, the difference in value of the ISC between the 84-octane gasoline and others is only S/0.09 (equivalent to 7.37%).

102. In the case of the third INC approved by MINAM (2020-2021 period) by Supreme Decree 007-2020-MINAM of August 18, 2020, there has been no subsequent regulatory development in terms of modification to the ISC by MEF, except for the latest regulation of April 2022. This means that the approval of the INC by MINAM does not necessarily lead to a process of review and modification of the ISC by MEF.

103. Based on the aforementioned point, it should be noted that both regulations, the one related to the INC issued by MINAM and the one related to the ISC issued by MEF are not integrated but rather are parallel to each other, which does not ensure effective compliance with the provisions of the Law of Sulfur Content in Diesel that provides that MEF should issue the tax regulations under its jurisdiction under the scope of what is stated in this Law.

104. In this sense, we consider relevant to present the interpretation related to the scope of Article 3 of the Law of Sulfur Content of Diesel as is indicated in the regulations issued by MEF for the regulation of the amounts of the ISC applicable to fuels.

105. In this regard, the following is stated in the explanatory memorandum of Supreme Decree No. 054-2009-EF of March 4, 2009, which modified Annex III that regulates the ISC for fuels:

> *“I. Background:*
> ***…as of the issuance of Law No. 28694, Law of Sulfur Content in Diesel, the Government has established that the objective of the tax policy regarding the Selective Consumption Tax (ISC) applicable to fuels, in the medium term, whether it is restructured based on the criterion of proportionality to the degree of noxiousness of the contaminants they contain for people's health,*** *so that the most polluting fuels - for example: residuals or diesel 2 , among others- bear a higher tax burden than less polluting ones – for example: liquefied petroleum gas (LPG) or vehicular natural gas (NGV), among others.*
> *This means that* ***the objective pursued by this legal norm was to provide that the users of polluting fuels begin to internalize the damage caused to the health of the population*** *through the aforementioned ISC – which aims to assess the negative externality generated –* ***and promote the use of less polluting fuels that would bear a lower tax burden for this tax.”***
>
> (emphasis our own).

106. In turn, the explanatory memorandum of Supreme Decree No. 322-2009-EF of December 31, 2009, the modifying legal regulation of Annex III that regulates the ISC for fuels, states that:

> *"I. **Background:***
> ***..., as of the issuance of Law No. 28694, the Government has established that the objective of the tax policy regarding the ISC) applicable to fuels in the medium term, is that it be restructured based on the criterion of proportionality to the degree of noxiousness that the fuel pollutants have on the health of the population** so that the most polluting fuels bear a higher tax burden than the less polluting ones.*
> *This means that the **objective pursued by this legal norm was to stipulate that the users of polluting fuels begin to internalize the damage caused to the health of the population through the aforementioned tax,** which aims to assess the negative externality generated by the consumption of this type of goods and value the negative externality generated by the consumption of this type of goods and promote the use of less polluting fuels, which would bear a lower tax burden for this tax."*
>
> (emphasis our own).

107. Similarly, the explanatory memorandum of Supreme Decree No. 013-2010-EF of January 22, 2010, modifying legal regulation of Annex III that regulates the ISC for fuels, states that:

> ***"From the proposal:***
> *Taking into account that there is technical evidence that Diesel No. 2 fuels with 50 ppm and Diesel No. 2 with more than 50 ppm do not have the same level of sulfur content (a highly polluting element); and, that Article 2 of Supreme Decree No. 061-2009-EM has established that a Diesel B2 with up to 50 ppm of sulfur content must be sold for automotive use in the province of Lima and in the Constitutional Province of Callao, **it is necessary to establish a different fixed amount of ISC for each one, which in turn must be lower for fuels that use Diesel with 50 ppm in order to comply with the provisions of Article 3 of Law No. 28694.***
> *In this sense, such differentiation of the Selective Consumption Tax applicable to said products takes into account the degree of noxiousness of the sulfur content, the behavior of the price of these products in the international market (Diesel 2 with 50 ppm and Diesel 2 with 2500 ppm), as well as its corresponding seasonality.*
> *Consequently, **to comply with the legal mandate contained in Article 3 of Law No. 28694, it is convenient to modify the ISC applicable** to the following goods in the New Appendix III of the Single Ordered Text (TUO) of the IGV and ISC Law..."*
> *(emphasis our own).*

108. In turn, the explanatory memorandum of Supreme Decree No. 265-2010-EF of December 24th, 2010, another norm that modifies Annex III that regulates the ISC for fuels, states:

> *“ **I. Background:***
> *…Article 3 of Law No. 28694, Law of Sulfur Content in Diesel, has provided that starting on January 1st, 2008, the ISC for fuels will be determined by introducing the criterion of proportionality into the degree of noxiousness that the pollutants have on the health of the population.*
> *In this sense, as of the issuance of Law No. 28694, the Law of Sulfur Content in Diesel, it has been established that starting on January 1st, 2008, the ISC for fuels will be determined by introducing the criterion of proportionality into the degree of noxiousness that the pollutants have on the health of the population.*
> *In this sense,* ***as of the issuance of Law No. 28694, the Government has stipulated that the objective of the tax policy regarding the ISC applicable to fuels, is that it be restructured based on the criterion of proportionality to the degree of noxiousness that the pollutants have on the health of the population so that the most polluting fuels bear a greater tax burden than the less polluting ones.***
> *This means that the objective pursued by the aforementioned legal norm was to stipulate that the users of polluting fuels begin to internalize the damage caused to the health of the population through the aforementioned tax – which aims to assess the negative externality generated by the consumption of this type of goods – and promote the use of less polluting fuels that would bear a lower tax burden for this tax.”*
>
> (emphasis our own).

109. Similarly, the explanatory memorandum of Supreme Decree No. 270-2010-EF of October 29, 2010, states the following:

> ***“I. Background:***
> ***…as of the issuance of Law No. 28694, Law of Sulfur Content in Diesel, the Government has stipulated that the objective of the tax policy regarding the Selective Consumption Tax (ISC) applicable to fuels in the medium term, is that it be restructured based on the criterion of proportionality to the degree of noxiousness that the fuel pollutants have on the health of the population so that the most polluting fuels*** *– for example: residuals or diesel 2 , among others – bear a higher tax burden than less polluting ones – for example: liquefied petroleum gas (LPG) or vehicular natural gas (NGV), among others.*

This means that the objective pursued by this legal norm was to stipulate that the users of polluting fuels begin to internalize the damage caused to the health of the population through the aforementioned ISC – which aims to assess the negative externality generated – and promote the use of less polluting fuels, which would bear a lower tax burden for this tax.
In this sense, in practice, this legal measure aims to act as a disincentivizing mechanism for the consumption of the most polluting fuels and to promote consumer substitution of consumption of these by other less polluting ones".

(emphasis our own)

110. As can be verified from the aforementioned quotes extracted from documents issued by MEF, there is a recurring reference that with the Law of Sulfur Content in Diesel the Peruvian Government adopted the legal mandate to apply the criterion of proportionality to the degree of noxiousness of the pollutants as a tax policy regarding matters of ISC applicable to pollutants. That is, the tax authority itself understands that its scope for regulating this tax must be subject to the application of the INC (the regulations issued by MINAM on this matter), as there is a legal norm with the rank of Law that establishes it. This is currently not happening. As a consequence of this finding there is a need for both Ministries to jointly review the existing regulatory scheme in order to ensure effective compliance with the environmental law under analysis.

111. Additionally, it should be noted here that, after reviewing the various modifications approved by MEF to regulate the ISC for fuels, one modification has been identified in which reference is made to a scale of noxiousness factors that were not formally approved (through Supreme Decree) and, rather, were sent by MINAM to MEF, via email (dated February 20, 2018). We refer to Supreme Decree No. 094-2018-EF of May 9, 2018. Indeed, the explanatory memorandum of this regulation mentions said scale that was sent electronically, which differs substantially from the scale formally approved by MINAM and that was in force at the time of issuing the indicated MEF Supreme Decree (we refer to Supreme Decree No. 006-2014-MINAM of May 1, 2014). Below is the content of the scale of noxiousness factors that, according to what was indicated by MEF, had been sent to them by email:

TABLE NO.2:
NOXIOUSNESS OF FUELS SUBMITTED BY MINAM TO MEF THROUGH EMAIL

Combustible	Factor de nocividad Total (gr/kg)
Gas Natural	4
Gas Licuado de Petróleo (GLP)	9
Gasohol 84 Octanos	116
Gasohol 90 Octanos	31
Gasohol 95/97/98 Octanos	20
Turbo A1	69
Diésel B5 - S50	46
Diésel B5 - S5000	56
Petróleo Industrial N° 6	105
Petróleo Industrial N° 500	143
Carbón antracítico	25
Carbón bituminoso	51

Fuente: MINAM (correo electrónico del 20.02.2018).

112. In relation to the last modification of the ISC approved by Supreme Decree No. 068-2022-EF (April 3, 2022), through which a set of fuels is exempted from the ISC, it is appropriate to point out what is noted in the explanatory memorandum of said regulation:

> *" I. **GROUNDS***
> *... it is important to highlight that in the function of the ISC its collection function prevails – which constitutes an important tax tool of the Tax System – which is to obtain the necessary resources to cover public spending. Likewise, it is an important tax instrument that helps to combat negative externalities, discourage, or modify the consumption of the goods on which it is applied.*
> *With regards to the purpose of specific taxes - such as the case of the ISC - as Fenochietto maintains, unlike the general ones, these not only have a collection purpose but also an extra-fiscal purpose that is to modify the consumption of certain goods and services through the internalization of the negative externalities or social costs that its consumption causes.*
> *(…)*

In the case of the ISC applicable to fuels, its purpose is to encourage the use of clean fuels, which makes it possible to reduce pollutant emissions and thus protect air quality and the health of the population. *The effect caused by fuels on health can be measured through noxiousness factors, among other factors, which measure the toxicity of emissions on human health and turn out to be a valid reference to determine the negative externality, among others, and, therefore, an adequate variable to establish criteria for determining the ISC of fuels"*

(emphasis our own).

113. Notwithstanding the above, this regulation (Supreme Decree No.068-2022-EF), at the same time, points to "the inflationary pressures that the country has been experiencing as a result of the international situation, mainly due to higher prices for fuels and imported food, in addition to the increase in international transportation logistics costs" as the basis to exclude a set of fuels (including both gasoline and diesel) from Appendix III, which regulates the IGV on fuels until June 30, 2022. This regulation, which could have been subject to extension, was not extended.

VII. CLOSING NOTE

1. Factual records provide information on the alleged lack to effectively enforce environmental laws pursuant to Articles 18.8 and 18.9 of the TPA and allows the public to draw its own conclusions regarding the enforcement of a particular environmental law by a Party, as well as providing valuable information to the Parties as they seek to meet their obligations under the TPA.

2. This factual record provides relevant information in accordance with the scope of the factual record referred to in paragraph IV.2 above.

3. This factual record was made public pursuant to Article 18.9.7. by instruction of the representatives of the Government of the United States in December 19, 2022.

December 19, 2022

Ms. Martha Aldana
Executive Director
Peru Secretariat for Environmental Enforcement Matters
Washington, D.C.

Dear Ms. Aldana:

The United States is pleased to receive the Factual Record resulting from the under Chapter 18 of the *United States-Peru Trade Promotion Agreement* (PTPA): Sulfur in Diesel Oil (SACA-SEEM/PE/002/2019). With this letter, the United States transmits its instruction to make the Factual Record publicly available in accordance with Article 18.9.7 of the PTPA.

Sincerely,

Kelly K. Milton
Assistant U.S. Trade Representative
Environment and Natural Resources
Office of the U.S. Trade Representative

Monica P. Medina
Assistant Secretary
Bureau of Oceans and International Environmental and Scientific Affairs
U.S. Department of State

U.S. Representatives of the PTPA Environmental Affairs Council

SENSITIVE BUT UNCLASSIFIED

Instruction to the United States-Peru Trade Promotion Agreement (PTPA) Secretariat for Environmental Enforcement Matters (SEEM) Regarding Submission SACA-SEEM/PE/002/2019 (Sulfur in Diesel Oil)

THE UNITED STATES OF AMERICA:

SUPPORTIVE of the process provided for in Articles 18.8 and 18.9 of the *United States-Peru Trade Promotion Agreement* (PTPA) regarding Submissions on Enforcement Matters and the preparation of factual records;

CONSIDERING Submission SACA-SEEM/PE/002/2019 (the "Submission") filed on July 25, 2019, and the response provided by Peru on June 1, 2020;

RECALLING the SEEM's determination on July 13, 2020, that the development of a factual record is warranted and the instruction by the United States on October 1, 2020, instructing the SEEM to prepare a factual record;

HAVING REVIEWED the Factual Record prepared by the SEEM for Submission SACA-SEEM/PE/002/2019; and

ACTING IN ACCORDANCE WITH Article 18.9.7 of the PTPA;

HEREBY INSTRUCTS the SEEM to make the final Factual Record for SACA-SEEM/PE/002/2019 publicly available.

Kelly K. Milton
Assistant U.S. Trade Representative
for Environment and Natural Resources
Office of the U.S. Trade Representative

Date: __December 18, 2022_____

Monica P. Medina
Assistant Secretary
Bureau of Oceans and International
Environmental and Scientific Affairs
U.S. Department of State

Date: December 19, 2022

U.S. Representatives to the PTPA Environmental Affairs Council

SENSITIVE BUT UNCLASSIFIED

VIII. DOCUMENTS CONSULTED

a) Regulation of National Standards of Environmental Quality of the Air. Supreme Decree No. 074-2001-PCM (February 6, 2001)
b) Decree of the Directive Council No. 018-2005-CONAM-CD (December 2, 2005)
c) Bill 12130/2004-CR “Bill that proposes that the Ministry of Energy and Mines force fuel market agents, especially refineries, to reduce excess sulfur in derivatives, such as diesel and gasoline, a situation that seriously affects the health of the Population” presented by Congressman Luis Heysen Zegarra (Peruvian Aprista Party) (December 10, 2004).
d) Opinion of the Energy and Mines Commission on Bills 12089, 12130, 12152, 12719 and 12798/2004-CR, approved by the Commission on April 27, 2005.
e) Diary of Debates of the Permanent Commission of the Congress of the Republic (2005-2005 period) (July 20, 2005).
f) Law No. 28694, Law of Sulfur Content in Diesel (March 22, 2006)
g) 1993 Political Constitution of Peru.
h) General Environmental Law. Law No. 28611 (October 13, 2005)
i) Framework Law of the National System of Environmental Management. Law No. 28245 (October 8, 2004).
j) National Environmental Policy. Supreme Decree No. 012-2009-MINAM (May 23, 2009). Repealed.
k) National Environmental Policy to 2030. Supreme Decree No. 023-2021-MINAM (July 25, 2021). Currently in force.
l) Legislative Decree No. 1013, Law of Creation, Organization, and Functions of the Ministry of the Environment (May 13, 2008).
m) Ley No. 26520. Organic Law of the Ombudsman's Office (28.09.1995).
n) Ley No. 27785, 27785, Law of the National Control System and the Comptroller General of the Republic (15.05.2018).
o) Report No. 271-2007-EF/66.01 of the General Directorate of Public Revenue Policy of the Ministry of Economy and Finance (September 21, 2007).
p) Supreme Decree No. 211-2007-EF that established fixed amounts of the Selective Consumption Tax considering the criterion of proportionality to the degree of noxiousness of fuels, in accordance with the provisions of Law No. 28694 (December 23, 2007).
q) Castro, Mariano (2010). "The integration of health and the environment in public policies: Avoiding air pollution". Scientific Magazine 7(2). Universidad Científica del Sur.
r) Official Letter No. 286-2008-EF/15 (October 21, 2008) from the Vice Minister of Economy to the Vice Minister of Environmental Management.
s) Official Letter No. 006-2009-EF/15.01 (January 9, 2009) from the Vice Ministry of Economy to the Vice Minister of Environmental Management.
t) Ombudsman Report No. 136, “Air Quality in Lima and its Impact on the Health and Life of its Inhabitants: Follow-up of Ombudsman Recommendations” (August 19, 2008).

u) Report No. 659-2011-CG/MAC-VE of the Comptroller General of the Republic (December, 2011).

v) Official Letter No. 0056-2009-DVMGA/MINAM (January 27, 2009) addressed by the Vice Minister of Environmental Management to the Vice Minister of Economy.

w) Supreme Decree No. 006-2014-MINAM (May 1, 2014) and its explanatory memorandum.

x) Supreme Decree No. 003-2018-MINAM (May 9, 2018) and its explanatory memorandum.

y) Report No. 185-2018-MINAM/SG/OGAJ of the General Office of Legal Counsel of the MINAM (March 8, 2018).

z) Supreme Decree No. 007-2020-MINAM (August 18, 2020) and its explanatory memorandum.

aa) Ombudsman Report No. 116, "Air Quality in Lima and its Impact on the Health and Life of its Inhabitants" (December 21, 2006).

bb) Single Ordered Text of the Law on General Sales Tax and Selective Consumption Tax, approved by Supreme Decree No. 055-99-EF (April 14, 1999). New Annex III and its modifications including their respective explanatory memorandums.