ENERGY SUBSIDIES AND THE INTERNATIONAL TRADE REGIME

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Scope of Energy Subsidies

- Energy subsidies are ‘any government action that concerns primarily the energy sector that lowers the cost of energy production, raises the price received by energy producers or lowers the price paid by energy consumers’ (IEA).
  - to promote energy security, employment and economic growth, foster innovation and achieve social and/or environmental goals
- Energy subsidies are subject to WTO disciplines, like the SCM Agreement.
  - Fossil fuel subsidies
  - Renewable energy subsidies

Fossil Fuel Subsidies

- UN SDG 12: rationalization of inefficient fossil fuel subsidies that encourage wasteful consumption ‘by removing market distortions . . . Including by restructuring taxation and phasing out those harmful subsidies . . . to reflect their environmental impacts’, taking fully into account development issues.
- Estimated amounts: $440 billion in 2021 (IEA), $697.2 billion in 2021 (OECD and IEA), and $5.9 trillion in 2020 (IMF).
  - IEA’s price-gap approach: difference between a fuel’s market price and its actual (lower) price charged to domestic consumers
  - OECD’s inventory approach: around 1,500 individual policy measures in fifty-one economies
  - IMF’s approach: pre-tax (price-gap) subsidies and post-tax subsidies (reflecting the cost of negative externalities)
- Fossil fuel subsidies on international agenda since 2009 (G20, APEC, G7 etc)
- G20: voluntary peer reviews of inefficient fossil fuel subsidies among its member countries.
- WTO discussions in some of its bodies
- WTO Fossil Fuel Subsidy Reform (FFSR) initiative launched in 2021 and covering about 50 members seeks ‘the rationalization and phase out of inefficient fossil fuel subsidies that encourage wasteful consumption along a clear timeline’ and, for this purpose, facilitates information and experience sharing to advance WTO discussion aimed at ‘achieving ambitious and effective disciplines’ on these subsidies.

Fossil Fuel Subsidies

- Some FTA provisions
  - E.g., New Zealand–UK FTA (2022) sets out concrete obligations of the parties to eliminate ‘harmful fossil fuel subsidies’, except those in support of ‘legitimate public policy objectives’ and end ‘unabated coal-fired electricity generation in their territories’.
- Negotiations on Agreement on Climate Change, Trade and Sustainability – launched in 2019 and currently involving New Zealand, Costa Rica, Fiji, Iceland, Norway and Switzerland – are likely to introduce disciplines to eliminate harmful fossil fuel subsidies.
- Limitations of the SCM Agreement
  - It has almost never been used to directly challenge fossil fuel subsidies due to the low push from interest groups and the reluctance of governments to take legal actions.
  - Most subsidies are consumption subsidies, available to energy-consuming industries across the board, and hence not ‘specific’ to be countered under the SCM Agreement.
  - Undervaluation of externalities associated with fossil fuels – classified as fossil fuel subsidies under the IMF methodology – is difficult to challenge under the SCM Agreement.

Fossil Fuel Subsidies

- Dual Pricing
  - Charging a lower price for product sold domestically than in export markets (due to, e.g., direct price controls or indirect measures, like export restrictions)
  - Previous attempts since the oil crises in the 1970s to discipline dual pricing in GATT/WTO failed
  - GATT Art XI ban on quantitative export restrictions (that can decrease domestic prices but increase world prices);
  - Some WTO members' commitments on export duties and dual pricing
  - In many other legal contexts, WTO law is weak in constraining dual pricing.
    - For example, dual pricing may qualify as a 'subsidy' in the form of, for instance, the government provision of a good (natural gas, oil, electricity, etc.) to downstream industries at a less-than adequate remuneration. However, the underselling of energy in this case would often benefit virtually any energy-using industry, which would make such scheme a non-specific subsidy out of the SCM Agreement's reach.
- SOEs
  - Through SOEs, governments control roughly 70 per cent of global oil and gas production and about 60 per cent of coal production and coalfired power plants worldwide.
  - SOEs as recipients and subsidy-providers
  - Appellate Body found that a public body 'must be an entity that possesses, exercises or is vested with governmental authority'.
    - This narrow interpretation -> practical difficulties of countering many favours by SOEs

Fossil Fuel Subsidies

- Horizontal Improvements
  - Enhancing transparency
    - ‘chronic low compliance’ of members (in 2021, 58 per cent of WTO members did not notify subsidies)
    - proposals on expanding Secretariat’s technical assistance and on ‘punitive’ administrative measures for non-notification
  - SOEs
    - CPTPP provisions as a model?
      - Parties must ensure that their SOE ‘acts in accordance with commercial considerations in its purchase or sale of a good or service’.
      - Unlike the SCM Agreement, the CPTPP does *not* require SOEs to be a public body and disciplines non-commercial assistance given *specifically* to SOEs.
  - Restricting dual pricing outright
    - E.g., EU-Ukraine Association Agreement’s ban on dual pricing on energy goods
- Sectoral Improvements
  - Need for new WTO disciplines prohibiting ‘inefficient fossil fuel subsidies that encourage wasteful consumption’
    - ‘top-down’ approach: to provide a blanket definition of the inefficient subsidies concerned and/or list some particular subsidy forms
    - ‘bottom-up’ approach: members decide for themselves what subsidies to include into this category, subject to periodic updates.

Renewable Energy Subsidies

- Clean energy has garnered much lower subsidies than dirty energy.
  - Green electricity promotion schemes
    - Feed-in pricing support schemes, quota obligations (e.g., renewable portfolio standards), competitive tendering/bidding procedures or auctions, net metering and net billing systems
  - Various subsidies for renewable energy goods etc.
- Unlike fossil fuel subsidies, renewable energy subsidies have already been targeted by 10 WTO disputes and many countervailing measures
  - Renewable energy and related technologies are produced in many countries -> higher probability for trade tensions
  - Green subsidies in all these WTO disputes had discriminatory local content requirements while this is generally not typical of fossil fuel subsidies.

Renewable Energy Subsidies

- Key Messages from WTO Jurisprudence
  - *Canada – Renewable Energy / Canada – Feed-in Tariff Program* (Appellate Body Reports):
    - A State intervention creating a new market does not ‘in and of itself’ provide a benefit, and hence a subsidy.
    - price comparisons within the renewable electricity market alone, rather than across the blended electricity market as a whole.
- Need for creating more policy space for renewable energy subsidies
  - Ongoing decarbonization actions against harmful fossil fuel subsidies will necessitate more policy space for renewable energy subsidies to replace fossil fuels.
    - Due restraint for renewable energy subsidies
    - Technology transfer exemption
    - Increasing thresholds for negligible subsidies
    - Application of general exceptions

Conclusion

- Energy subsidies create cost (or price) advantages for beneficiary producers to the detriment of competitors.
- The SCM Agreement applies to both dirty and clean energy alike.
- But the actual SCM practice presents negative environmental implications for State energy promotion.
  - limitations of the WTO subsidy regime in effectively curtailing fossil fuel subsidies vs contrasting upward trend in attacking clean energy subsidies
- Thus, the WTO should readjust the existing subsidy rules to more effectively align with the environmental sustainability needs.

Source: *Energy and the Environment: Exploring the Nexus under International Economic Law* (Cambridge University Press, 2024)

- 'This is the most comprehensive treatment of the regulation of energy from an environmental perspective so far. The legal and economic logic of interventions in both the trade as well as the investment spheres is brought into light through the very competent writing of the author, who must also be complemented for expressing in a clear-cut understandable manner a very demanding topic. A book that no academic or practitioner working in this area can afford to overlook.' Petros C. Mavroidis, Edwin B. Parker Professor of Foreign and Comparative Law, Columbia Law School

  'This book offers a groundbreaking perspective by interlinking energy policy with environmental legal principles. Shadikhodjaev's unique approach lies in merging these often distinct fields, providing new insights into how international legal frameworks can address environmental challenges arising from energy consumption. This pioneering analysis, which critically evaluates existing legal structures and proposes innovative solutions for integrating energy policies with environmental protection, marks a significant contribution to the evolving international legal narrative. Shadikhodjaev's work sets a precedent in the field, serving as a vital guide for future policy and legal development.' Julien Chaisse, Professor of Law, City University of Hong Kong & President, Asia Pacific FDI Network