

# The Inadequacy of EU State Aid Law and WTO Law on Subsidies to Regulate Energy Tax Reliefs

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*The main objective of this paper is to assess whether EU State aid and WTO law on subsidies are effective and useful tools to regulate the use of energy tax reliefs, encompassing both allegedly 'positive' (i.e. environmental) aid measures as well as 'negative' (i.e. polluting) aid measures. Considering the need to face today's environmental challenges, this paper relies on the assumption that energy tax reliefs in favour of environmentally friendly energy sources should be promoted where energy tax reliefs that no longer match today's environmental challenges should be discouraged. This article analyses the extent to which current EU State aid and WTO law on subsidies put limit on the adoption of energy tax reliefs, either in favour of polluting energy sources or in favour of environmentally friendly energy sources. Finally, it reflects on the need to develop more consistent energy tax policies with regard to EU environmental and energy objectives.*

*Keywords: Energy Tax Relief; Green Subsidy; Energy-specific State aid and Subsidy Framework.*

## I. Introduction

Although countries tend to recognise the need to reduce the use of polluting energy sources, today's world economy still largely relies on the combustion of fossil fuels.<sup>1</sup> At the EU level, fossil fuel remains the main source of electricity (around 50%).<sup>2</sup> At the global level, the share of fossil fuel in electricity generation is even higher (around 67%).<sup>3</sup> At the same time, countries increasingly tend to encourage the

production and consumption of renewable energy sources.<sup>4</sup> In the EU, the Renewable Energy Directive sets a "target of at least 20% share of energy from renewable sources in the Community's gross final consumption of energy in 2020".<sup>5</sup> In November 2016, the Commission proposed to revise this Directive, setting a target of 27%, requiring Member States to collectively ensure that this target is reached.<sup>6</sup>

Despite the political calls in favour of renewable energy and the recognition of the negative impact of so-

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1 In 2009, OECD countries recognised the need to remove "environmentally harmful policies [...] such as subsidies: to fossil fuel consumption" (OECD, Declaration on Green Growth adopted at the Meeting of the Council at Ministerial Level on 25 June 2009) [C/MIN(2009)5/ADD1/FINAL], 2. See also OECD-IEA Fossil Fuel Support and Other Analysis, available at <http://www.oecd.org/site/tadffss/> Last accessed on 13 December 2016.

2 Eurostat, Environmental Data Centre on Natural Resources, available at <http://ec.europa.eu/eurostat/web/environmental-data-centre-on-natural-resources/natural-resources/energy-resources/fossil-fuels> Last accessed on 13 September 2016. Eurostat defines fossil fuels as follows: "Fossil fuel is a generic term for non-renewable carbon-based energy sources such as solid fuels, natural gas and oil that have their origins in plants and animals

that lived millions of years ago on earth and underwent transformation through chemical and physical processes."

3 International Energy Agency, Key World Energy Statistics (2016), available at <https://www.iea.org/publications/freepublications/publication/KeyWorld2016.pdf> Last accessed on 13 December 2016.

4 See e.g. at the EU level, EU's energy policy, available at <https://ec.europa.eu/energy/en/topics/energy-strategy> Last accessed 13 September 2016.

5 Directive 2009/28/EC of the European Parliament and of the Council of 23 April 2009 on the promotion of the use of energy from renewable sources and amending and subsequently repealing Directive 2001/77/EC and 2003/30/EC, OJ 2009 L 140/16. See Article 3 of the Directive.

6 European Commission, Proposal for a Directive of the European Parliament and of the Council on the Promotion of the use of energy from renewable sources (recast), COM(2016) 767 final.

cities based on fossil fuels' consumption, many countries keep – ambiguously and inconsistently<sup>7</sup> - supporting fossil fuels through preferential legislations, such as for example direct budgetary supports or 'tax expenditures'.<sup>8</sup> Yet, tax expenditures – defined by the OECD as "relative preferences within a country's tax system that are measured with reference to a benchmark tax treatment set by that country" - are difficult to reconcile with the environmental objective of reducing the use of fossil fuels and should therefore be avoided.<sup>9</sup>

The inconsistency of Member States' policy is not only national: the Energy Tax Directive (ETD) also proves not to be fully consistent with EU's environmental objectives. The ETD indeed sets minimum tax levels for energy products, which do not reflect their negative impact on climate change. Consequently, if Member States follow these minimum tax levels, energy products with a high climate change impact could be subject to lower tax rates than products with a much lower impact.<sup>10</sup>

Yet, taxation of energy products can be an instrument for achieving a more sustainable society, either by means of tax disincentives to discourage the use of 'polluting' energy sources or by means of tax advantages to encourage the use of 'clean' energy sources. For example, the EU Renewable Energy Directive includes 'tax exemptions or reductions' and 'tax refunds', among the 'support schemes' that Member States may use to achieve their national renewable energy targets.<sup>11</sup> Where it is true that tax policy is certainly not

the only factor influencing the price of energy products, taxation is certainly one instrument, among others, that can be used to make the price of energy products better reflect their environmental cost.<sup>12</sup>

Considering the potential role of taxation in meeting contemporary environmental challenges, including climate change, this article looks at EU State aid law and WTO law surrounding subsidies as potential instruments to ensure that the use of energy taxation by EU Member States and WTO Members is consistent with the assumption that harmful (fossil fuel) subsidies should be discouraged while allegedly positive environmental subsidies should either be promoted or, at least, not be hampered. EU State aid law and WTO law surrounding subsidies – in particular, the Agreement on Subsidies and Countervailing Measures (ASCM) - indeed limit the way States may or not adopt preferential (tax) measures in favour of certain sectors.

The Commission, by issuing guidelines on State aid for environmental protection and energy, has made clear that EU State aid law – and consequently, the Commission's interpretation of State aid provisions - may impact Member States' environmental policies based on aid measures, such as tax incentives.<sup>13</sup> Similarly, the Commission has included, in the General Block Exemption Regulation (GBER) that declares certain categories of aid compatible with the internal market, a direct reference to "aid in the form of reductions in environmental taxes under Directive 2003/96/EC", which also indicates that Member

7 J Sauvage, 'Tackling the folly of fossil fuel subsidies' (2015) 304 OECD Observer, available at <[http://www.oecdobserver.org/news/fullstory.php/aid/5295/Tackling\\_the\\_folly\\_of\\_fossil\\_fuel\\_subsidies.html](http://www.oecdobserver.org/news/fullstory.php/aid/5295/Tackling_the_folly_of_fossil_fuel_subsidies.html)> Last accessed on 12 September 2016.

8 See e.g. the report of Friends of Europe and CEE Bankwatch Network, 'Climate's Enfants Terrible: How New Member States' Misguided use of EU Funds is Holding Back Europe's Clean Energy Transition', available at <<http://bankwatch.org/enfants-terribles>> Last accessed on 12 September 2016); Carbon Market Watch, 'Fossil fuel subsidies from Europe's Carbon market: The lessons learnt with article 10c of EU ETS Directive and Recommendations for the post 2020 period', April 2016, available at <<http://carbonmarketwatch.org/wp-content/uploads/2016/04/Fossil-fuel-subsidies-from-Europes-carbon-market-final-web.pdf>> Last accessed on 13 September 2016. Some NGOs have called for the end of fossil fuel subsidies, see e.g. the work of the Climate Action Network Europe on fossil fuels, available at <<http://www.caneurope.org/policywork/fossil-fuel-subsidies>> Last accessed on 13 September 2016. See also F Oosterhuis, H Ding, L Franckx, P Razzini and Member States Experts, European Commission final report, Enhancing comparability of data on estimated budgetary support and tax expenditures for fossil fuels, 2014.

9 OECD, Inventory of Estimated Budgetary Support and Tax Expenditures for Fossil Fuels 2013 (OECD Publishing 2013). According to the OECD, "Since the benchmark or "normal" tax treatment varies considerably from country to country, the value of this type of support is not comparable across countries. Thus, for example,

a country that applies high rates of taxation to fossil-fuel end products within the context of an excise-tax system with lower rates for some products than others may have higher measured support to fossil fuels than a country with lower but uniform excise-tax rates, even if the tax system of the former country has higher taxes than the latter country on each type of fuel" (p.16). See also OECD, Companion to the Inventory of Support Measures for Fossil Fuels 2015, available at <<http://www.oecd.org/site/tadffss/publication/>> Last accessed on 13 September 2016; OECD and selected partner economies, Taxing Energy Use 2015 (OECD Publishing 2015), available at <<http://www.oecd.org/tax/taxing-energy-use-2015-9789264232334-en.htm>> Last accessed on 13 September 2016.

10 See European Commission, Proposal for a Council Directive amending Directive 2003/96/EC restructuring the Community framework for the taxation of energy products and electricity, COM (2011) 169 final, 3. This Proposal was withdrawn (OJ C 80/17).

11 Article 2(k) of the *Directive 2009/28/EC* (n 5).

12 See e.g. S Tumen, D Unalmis, I Unalmis and D F Unsal, 'Taxing Fossil Fuels under Speculative Storage' (2014) IMF Working Paper, WP/14/228.

13 See European Commission, Guidelines on State aid for environmental protection and energy 2014-2020, OJ C 200. ('2014 Guidelines')

States' energy tax policy – which should be in line with EU State aid law – may be influenced by the Commission's understanding of what can “indirectly benefit the environment”.<sup>14</sup> EU case-law also proves that the Court of Justice may play a role in assessing the consistency of Member States' energy tax policy with EU State aid law.<sup>15</sup> For example, in the *Adria-Wien Pipeline GmbH* case, the Court of Justice of the European Union considered that the rebate of energy taxes in favour of certain undertakings only (*de facto* ‘undertakings whose activity is shown to consist primarily in the manufacture of goods’) constituted incompatible State aid.<sup>16</sup> The Court considered the environmental rationale of the tax rebate and found that this justification was not consistent with the way the measure was designed.<sup>17</sup> The Court pointed out that the rebate only benefited undertakings manufacturing goods (in contrast to undertakings supplying services), while “energy consumption by each of those sectors is equally damaging to the environment”.<sup>18</sup>

At the WTO law level, disputes on energy subsidies have been analysed under the General Agreement on Tariffs and Trade (GATT Articles VI, XVI and XX) but also under the Agreement on Subsidies and Countervailing Measures (ASCM), which high-

lights that WTO law concerning the adoption of subsidies may also function as a legal barrier against the adoption of certain categories of aid measures in favour of the energy sector, including energy tax reliefs.<sup>19</sup> For example, in the cases *Canada – Feed-In Tariff Program* and *Canada – Renewable energy*, Japan and the European Union challenged the compatibility of a programme of the Province of Ontario in Canada guaranteeing a minimum price to “generators of electricity produced from certain forms of renewable energy” with the ASCM.<sup>20</sup> The ASCM was also invoked by the US in its first request for consultation in the case *India – Certain Measures relating to Solar Cells and Solar Modules*.<sup>21</sup> This claim was however not analysed by the Panel and Appellate Body as the US did not refer to the ASCM in its second request.<sup>22</sup> Yet, the potential burden of WTO rules surrounding subsidies on WTO Members that intend to adopt energy tax reliefs cannot be put into question.

The second and third section of this article aim to assess whether the burden created by EU State aid law and WTO law surrounding subsidies on Member States' energy tax policy may be a tool to guide Member States' energy tax policy towards more consistency with today's global environmental challenges. The analysis looks both at tax reliefs in favour of polluting energy sources (section 2) and tax reliefs in favour of environmentally friendly energy sources (section 3). In other words, EU State aid law and WTO law surrounding subsidies are analysed in the light of two different objectives. First, section 2 discusses whether EU State aid law and WTO law surrounding subsidies may be adequate legal instruments to satisfactorily regulate energy tax reliefs in favour of polluting energy sources. Then, section 3 focuses on the role of EU State aid law and WTO law surrounding subsidies to encourage – or at least not discourage – the adoption of allegedly positive energy tax reliefs.

## II. The Case of Polluting Energy Sources

As mentioned *supra*, EU State aid law and WTO law surrounding subsidies both limit the way States may or not adopt preferential (tax) measures in favour of certain sectors. Though they present significant similarities, both regimes are independent from each other, making it interesting to analyse both of them in parallel. Although the goal of this article is not to provide a detailed comparison of the two regimes, it may be

14 European Commission, Regulation No. 651/2014 of 17 June 2014 declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 of the Treaty, OJ 2014 L187/1. ('GBER'). See Article 44 and recital 64 of the GBER.

15 For a detailed analysis of the case-law, see M Villar Ezcurra, 'Energy Taxation and State Aid Law' in I Richelle, W Schön and E Traversa (eds), *State Aid Law and Business Taxation*, (Springer 2016), 213-217.

16 Case C-143/99, *Adria-Wien Pipeline und Wietersdorfer & Pegauer Zementwerke* [2001] ECLI-598.

17 *Ibid.*, [52].

18 *Ibid.*

19 See e.g. the cases WTO, Appellate Body, *Canada – Certain Measures Affecting the Renewable Energy Generation Sector*, 6 May 2013, DS412, 416; WTO, Panel Report, *India – Certain Measures relating to Solar Cells and Solar Modules*, 24 February 2016, WT/DS456/R.

20 WTO, Appellate Body, *Canada – Certain Measures Affecting the Renewable Energy Generation Sector*, 6 May 2013, DS412, 416. See F Ramírez Carmona, 'The Feed-in Tariffs Entanglement: A Comparative Study of the Analytical Approaches Followed by the EU and WTO Judiciary Bodies regarding Renewable Energy Subsidies' (2016) 43(2) *Legal Issues of Economic Integration*, 201.

21 See WTO, Request for consultations by the United States, *India – Certain Measures relating to Solar Cells and Solar Modules*, 11 February 2013, WT/DS456/1. See also footnote No.1 of the Panel Report: WTO, Panel Report, *India – Certain Measures relating to Solar Cells and Solar Modules*, 24 February 2016, WT/DS456/R.

22 Footnote No.1 of the Panel Report: WTO, Panel Report, *India – Certain Measures relating to Solar Cells and Solar Modules*, 24 February 2016, WT/DS456/R.

useful to briefly recall some of their main features. Both regimes aim at the protection of undistorted trade: EU State aid law aims at guaranteeing the functioning of the internal market while WTO law on subsidies pursues the objective of avoiding the distortion of free trade.<sup>23</sup> To achieve these goals, certain types of aid measures are forbidden. EU State aid law deems incompatible with the internal market “any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States” (Article 107 TFEU). WTO law surrounding subsidies uses similar conditions to define the subsidies it controls. The ASCM prohibits WTO Members to adopt “prohibited subsidies” (defined as “subsidies contingent upon export performance or contingent upon the use of domestic goods”) as well as specific subsidies that cause adverse effects to the interests of other WTO Members.<sup>24</sup>

None of the two regimes aim at protecting the environment or pursuing other specific non-trade objectives. Both EU State aid law and WTO law on subsidies aim at controlling potentially distortive aid measures. Legally speaking, ‘potentially distortive aid measures’ are defined under EU State aid law and WTO law on subsidies by reference to the conditions listed under Article 107 of the TFEU and the ASCM, respectively. These conditions are summarised in Table 1.<sup>25</sup>

Logically, EU State aid law and WTO law surrounding subsidies only permit to control energy tax reliefs in favour of fossil fuels when they fall under their scope. They do not provide for a systematic control of such tax measures. Consequently, as long as energy tax reliefs are designed in such a way so as to escape from the control of EU State aid law and WTO law on subsidies, they will be deemed compatible with the internal market and international trade, regardless of the fact that they potentially encourage polluting behaviours. For example, the establishment of lower rates of excise duties on energy products for commercial use would not be subject to the control of EU State aid law and WTO law surrounding subsidies, given the general character of such measures. The mere fact that polluting energy sources would benefit from tax reliefs does not lead to their incompatibility with EU State aid law or WTO law surrounding subsidies.

Under WTO law, the unsystematic character of the control on aid measures is even stronger. Indeed, there is no similar *ex ante* control under WTO law as it is

the case under EU law through the approval by the Commission of aid schemes. The control must always be triggered by the action of a WTO Member that considers to be affected by a subsidy adopted by another WTO Member.<sup>26</sup> Furthermore, the last years, most disputes on energy issues at the WTO level concerned preferential measures to the renewable energy sector (not to fossil fuels), which indicates that WTO Members have not been very active so far in putting into question potentially distortive measures in favour of fossil fuels.<sup>27</sup> Some authors nevertheless consider that “the WTO offers an appropriate forum for addressing issues relating to such harmful [fossil fuel] subsidies”, encouraging NGOs to notify such harmful subsidies to WTO Trade Policy Review Body.<sup>28</sup>

Though EU State aid law and WTO law may serve to catch certain types of harmful energy subsidies, neither EU State aid law nor WTO law surrounding subsidies are adequate instruments to control, in a systematic way, Member States’ policies in favour of fossil fuels.<sup>29</sup> *Ad hoc* instruments should be designed to regulate the use of such harmful subsidies.<sup>30</sup> In the

23 For a detailed comparison, see C Micheau, *State Aid, Subsidy and Tax Incentives Under EU and WTO Law* (Kluwer Law International 2014); L Rubini, *The Definition of Subsidy and State Aid. WTO and EC Law in Comparative Perspective* (OUP 2009); P Wegener Jessen, ‘Rules on state aid and subsidies’, in S E Gaines, B Egelund Olsen and K Engsig Sorensen (eds), *Liberalising Trade in the EU and the WTO: A Legal Comparison* (CUP 2012), 288-308.

24 See Articles 1 to 5 of the ASCM.

25 The table has been largely inspired by the comparison made by Pernille Wegener Jessen (n 23) in the article referred above.

26 See, however, Article 25 of the ASCM (‘notifications’).

27 See P D Farah and E Cima, ‘Energy Trade and the WTO: Implications for Renewable Energy and the OPEC Cartel’ (2013) *Journal of International Economic Law*, 1-34. See also, on the role of WTO law in limiting fossil fuel subsidies, R Steenblik, ‘17. Subsidies in the Traditional Energy Sector’ in J Pauwelyn (ed.), *Global Challenges at the Intersection of Trade, Energy and the Environment* (The Graduate Institute Centre for Trade and Economic Integration 2010), 182-192.

28 L Casier, R Fraser, M Halle and R Wolfe, ‘Shining a Light on Fossil Fuel Subsidies at the WTO: How NGOs can contribute to WTO notification and surveillance’ (2014) GSP Report, International Institute for Sustainable Development, 4.

29 A same reasoning has been followed by Traversa and Flamini with regard to the role of State aid in tackling harmful tax competition: E Traversa and A Flamini, ‘Fighting Harmful Tax Competition through EU State Aid Law: Will the Hardening of Soft Law Suffice?’ (2015) 3 *EStAL*, 323, 326: “In fact, State aid provisions are not a suitable instrument for tackling harmful tax competition, not only because of the wording of article 107 TFEU, but also because of the nature of State aid control: namely, it is based on a case by case approach, it is limited to the territory of one Member State and it does not take into consideration other Member State’s practices”.

30 I Espa and S E Rolland, ‘Subsidies, Clean Energy, and Climate Change’ (2015) 215 *Task Force on Rethinking International Subsidies Disciplines*, ICTSD, World Economic Forum.



Table 1

	EU State Aid Law	WTO Law (ASCM)
<b>Conditions</b>	(i) Aid (economic benefit) (ii) Granted by a Member State or through State resources <sup>1</sup> (iii) Advantage to certain undertakings or the production of certain goods <sup>2</sup> (iv) Measure distorts (or threatens to distort) competition (v) affects trade between Member States <sup>3</sup>	(i) Financial contribution or income/price support (economic benefit) <sup>4</sup> (ii) Granted by a government or public body <sup>5</sup> (iii) prohibited subsidies: <sup>6</sup> <i>per se</i> incompatible (export subsidies and subsidies contingent upon the use of domestic products) (iiib) actionable subsidies: <sup>7</sup> <ul style="list-style-type: none"> <li>• Specific to an enterprise or industry or group of enterprises or industries<sup>8</sup></li> <li>• Measure causes adverse effects on trade between Members</li> </ul>

Source: Author's own compilation, inspired by Wegener Jessen (n 23).

- 1 On the interpretation of this condition, see C-379/98 PreussenElektra AG [2001] ECLI-160, [60-61]; C-262/12 Vent de Colère [2013] ECLI-851, [34-37]; C-206/06 Essent Netwerk Noord BV [2008] ECLI-413, [74].
- 2 See C-5/14 Kernkraftwerke Lippe-Ems GmbH [2015] ECLI-354 (on whether a duty imposed on the use of nuclear fuels for the commercial production of selectivity constitutes State aid). The CJEU considered that “methods of producing electricity, other than that based on nuclear fuel [...] are not [...] in a factual and legal situation that is comparable to that of the production method based on nuclear fuel” (para. 79).
- 3 J Englisch, ‘EU State Aid Rules Applied to Indirect Tax Measures’ (2013) 1 EC Tax Review 9, 16: “according to settled case law of the ECJ, it is not necessary to establish that the fiscal aid has a real effect on trade between Member States and that it actually distorts or threatens to distort competition”. According to J Maïllo, “It is also important to consider that while at the beginning the focus of EU State aid control was on avoiding discrimination against foreign producers and distortions of trade between Member States, the focus has progressively moved to detect unequal treatment between companies operating in the same Member State (more intra-State than inter-State situations).” J Maïllo, E Traversa, J Corti and A Pirlot, ‘EU Energy Taxation System & State aid control. Critical analysis from competitiveness and environmental protection objectives’ (2016) 53 CEU Serie Política de la Competencia, 9.
- 4 Article 1.1.1. of the ASCM.
- 5 Article 1.1.1. of the ASCM.
- 6 Article 3 of the ASCM. See the illustrative list of export subsidies (Annex I of the ASCM).
- 7 Article 5 of the ASCM.
- 8 Article 2 of the ASCM.

next section, the analysis turns to an examination of energy tax reliefs in favour of environmentally friendly energy sources, such as renewable energy sources.

### III. The Case of ‘Environmentally Friendly’ Energy Tax Reliefs

Environmentally friendly energy tax reliefs are often designed as ‘specific’ measures. They may for exam-

ple provide preferential tax treatment to producers of renewable energy sources, excluding producers of ‘traditional’, non-renewable energy sources, from the preferential treatment. They may also provide preferential tax treatment under the conditions that the energy is produced at the local level, with local products (e.g. solar panels produced in the EU).<sup>31</sup> Once such measures fall under the control of EU State aid law or WTO law on subsidies, the question arises as to whether these two legal instruments leave sufficient room for manoeuvre to Member States in order to adopt energy tax reliefs in favour of renewable energy sources and whether the control operated is consistent with environmental considerations.

#### 1. EU State Aid Law<sup>32</sup>

In principle, Member States are obliged to notify the Commission when they plan to grant aid measures

31 Cases where domestic products are favoured over imported products may not only fall under the control of State aid/subsidies but also under Article 110 of the TFEU as well as GATT Articles II:2(a) and III:2, which formulate a non-discrimination principle.

32 This part is partly inspired by an article written in the framework of the Jean Monnet Project lead by Prof Marta Villar Ezcurra: A Pirlot, ‘WTO law and State aids on energy tax reliefs: common grounds and differences’ in M Villar Ezcurra (ed.), *State Aids, Taxation and the Energy Sector* (Thomson-Reuters-Aranzadi, 2017 forthcoming).

(Article 108 (3) TFEU). The Commission then decide whether the aid is compatible or not with the internal market, considering Articles 107 to 109 of the TFEU as well as EU law provisions relevant to the aid that has been notified. Aid measures in the form of tax reliefs in favour of environmentally friendly energy taxes are subject – in addition to EU’s general provisions surrounding State aid (Articles 107 to 109 TFEU) – to two main sets of rules: the GBER and the Commission Guidelines on State aid for environmental protection and energy 2014-2020.<sup>33</sup> These two sets of rules include provisions referring to a category of aid that may encompass ‘energy tax reliefs’, namely “aid in the form of reductions in or exemptions from environmental taxes”.<sup>34</sup>

First, Article 44 of EU’s GBER lays down a presumption of compatibility with State aid law and an exemption from the notification requirement in the case of aid schemes in the form of reduction in environmental taxes fulfilling the conditions of the ETD. The application of Article 44 is subject to two main substantive conditions: (i) the minimum taxation levels required by the ETD should be met and (ii) the beneficiaries of the tax reduction should be chosen in a transparent and objective way.

Second, as mentioned above, the European Commission has issued guidelines that help to assess under which conditions “aid for environmental protection and energy” may be compatible with EU State aid law.<sup>35</sup> Among the various aid schemes analysed, the guidelines also deal with “aid in the form of reductions in or exemptions from environmental taxes and in the form of reductions in funding support for electricity from renewable sources”.<sup>36</sup> In the case of “harmonized environmental taxes”, the guidelines provides that “aid in the form of tax reductions” will be considered “necessary and proportional” under the same two requirements as the one mentioned in Article 44 of the GBER and under the additional condition that the “aid is granted in principle in the same way for all competitors in the same sector, if they are in a similar factual situation”.<sup>37</sup>

Taking into consideration the GBER and the Commission Guidelines, Member States may adopt tax reliefs in favour of environmentally friendly energy sources if they respect the conditions mentioned therein. These substantive conditions have no direct link with the environmental objective pursued by the tax reliefs under control. Under the GBER, Article 44 does not require that the measure helps to foster en-

vironmental protection.<sup>38</sup> Similarly, an aid measure does not need to pursue an environmental objective to fall under the Commission’s guidelines. The reference in the GBER and in the guidelines to the concept of ‘environmental tax’ does not imply that the tax fulfils an environmental objective as this concept is defined in a very broad way. The GBER and the guidelines indeed define the concept of “environmental tax” as “a tax with a specific tax base that has a clear negative effect on the environment or which seeks to tax certain activities, goods or services so that the environmental costs may be included in their price and/or so that producers and consumers are oriented towards activities which better respect the environment”.<sup>39</sup>

All in all, the primary objective of aids in the form of reduction from environmental taxes seems to be the prevention that a Member State is discouraged from adopting an environmental tax due to the potential negative impact that such tax could have on the competitiveness of certain sectors.<sup>40</sup> For this reason, aid schemes – which are deemed to be ‘environmental’ under the GBER and the guidelines – could *de facto* amount to energy tax reliefs in favour of highly polluting industries or highly polluting energy sectors.

The absence of environmental requirement in the GBER and the guidelines regarding the assessment of energy tax reliefs may be criticised, not only because it leaves room for environmentally harmful tax

33 See 2014 Guidelines (n 13) and GBER (n 14). On the legal status of the GBER and the Guidelines, see M Villar Ezcurra, ‘EU State Aid and Energy Policies as an Instrument of Environmental Protection: Current State and New Trends’ (2014) 4 EStAL, 665, 670.

34 See 2014 Guidelines (n 13) and GBER (n 14).

35 See 2014 Guidelines (n 13).

36 See 2014 Guidelines (n 13), section 3.7.

37 See 2014 Guidelines (n 13), [173], section 3.7.1.

38 See also Article 6 (4) (e) of the GBER that indicates that “aid in the form of reductions in environmental taxes under Directive 2003/96/EC, if the conditions laid down in Article 44 of this Regulation are fulfilled” “are not required to have or shall be deemed to have an incentive effect”.

39 See 2014 Guidelines (n 13), [15] and Article 2 (119) GBER (n 14).

40 2014 Guidelines (n 13), [167]. The paragraph provides that: “while reductions in or exemptions from environmental taxes may adversely impact that objective [i.e. their environmental objective], such an approach may nonetheless be needed where the beneficiaries would otherwise be placed at such a competitive disadvantage that it would not be feasible to introduce the environmental tax in the first place”. See also the analysis by P Nicolaides and M Kleis, ‘A Critical Analysis of Environmental Tax Reductions and Generation Adequacy Provisions in the EEAG 2014-2020’ (2014) 4 EStAL, 636, 640-642.

reliefs to be found compatible with EU State aid law but also because it could potentially limit the possibility of Member States to adopt genuine, well thought out environmentally friendly energy tax reliefs. It also provides one more indication that EU State aid law is not an adequate tool to regulate Member States' energy tax policy.

## 2. WTO Law Surrounding Subsidies

In contrast with EU State aid law, the ASCM does not contain any specific provisions regarding environmental subsidies.<sup>41</sup> Initially, the ASCM contained a provision allowing WTO Members to adopt certain subsidies in light of their purpose of general interest (Article 8 of the ASCM), including subsidies to promote "adaptation of existing facilities to new environmental requirements".<sup>42</sup> This provision has nevertheless expired in 1999.<sup>43</sup> Consequently, a tax relief in favour of environmentally friendly energy sources would only pass the test of the ASCM if the measure is designed so as not to be characterised as a 'prohib-

ited subsidy' or as an 'actionable subsidy'. In other words, the conditions for environmentally friendly energy tax reliefs would be identical to the ones that apply to environmentally harmful tax reliefs.

Despite the lack of specific provisions in the ASCM, some authors argue that energy tax reliefs aimed at environmental purposes could be justified based on Article XX of the GATT.<sup>44</sup> GATT Article XX - which is GATT general exceptions provision - permits to justify measures, which would *a priori* contradict other GATT provisions, by reference to their purpose. Measures falling under GATT Article XX include measures "necessary to protect human, animal or plant life or health" (paragraph b) as well as measures "relating to the conservation of exhaustible natural resources" (paragraph g). Given that the ASCM does not contain any specific references to GATT Article XX, it is nevertheless unlikely that this provision may be applied to situations considered to violate provisions of the ASCM.<sup>45</sup>

Yet, the case-law suggests that environmental factors may be considered in the assessment of subsidies under WTO law. Indeed, the disputes *Canada – Feed-in tariff Program* and *Canada - Renewable energy*, seem to indicate that Panels and Appellate Bodies tend to regard environmental objectives in the evaluation of favourable (tax) measures.<sup>46</sup> These cases suggest that the specific features of the renewable energy market played a role in the assessment of the WTO compatibility of feed-in tariffs in favour of generators of renewable electricity. The Appellate Body, in a seemingly contradictory manner, stated in its report, as follows:

Nevertheless, while introducing legitimate policy considerations into the determination of benefit cannot be reconciled with Article 1.1.(b) of the SCM Agreement, we do not think that a market-based approach to benefit benchmarks excludes taking into account situations where governments intervene to create markets that would otherwise not exist.<sup>47</sup>

This quote expresses the idea that the Appellate Body recognises the possibility for governments to adopt policy measures in order to support sectors, such as for example the renewable energy sector, that are not directly competitive without government intervention. So far, in absence of clear WTO rules surrounding incentives schemes aimed at protecting the environment, the risk however remains that energy tax

41 See however the WTO Agreement on Agriculture (in particular Annex II).

42 See S Charnovitz, 'Green Subsidies and the WTO' (2014) World Bank Group, Policy Research Working Paper 7060, 56.

43 See Article 31 of the ASCM.

44 See *Farah/Cima* (n 34), 21-22; P D Farah and E Cima, 'WTO and Renewable Energy: Lessons from the Case Law' (2015) 49(6) *Journal of World Trade*, 1103, 1113-1115.

45 See G Marceau and J P Trachtman, 'A Map of the World Trade Organization Law of Domestic Regulation of Goods: The Technical Barriers to Trade Agreement, the Sanitary and Phytosanitary Measures Agreement, and the General Agreement on Tariffs and Trade' (2014) 48(2) *Journal of World Trade*, 364; C Tran, 'Using GATT, Art XX to justify climate change measures in claims under the WTO Agreements' (2010) 27 *Environmental and Planning Law Journal*, 346, 354 and 356-358; S Zleptnig, *Non-Economic Objectives in WTO Law. Justification Provisions of GATT, GATS, SPS and TBT Agreements* (Martinus Nijhoff Publishers 2010), 1214. See also WTO, Appellate Body Report, *China – Measures related to the exportation of various raw materials*, 30 January 2012, WT/DS394/AB/R, WT/DS395/AB/R, WT/DS398/AB/R (*China – Raw Materials*), para. 303; WTO, Appellate Body Report, *China – Measures affecting trading rights and distribution services for certain publications and audiovisual entertainment products*, 21 December 2009, WT/DS363/AB/R (*China – Publications and Audiovisual Products*), para. 229-230.

46 WTO, Appellate Body, *Canada – Certain Measures Affecting the Renewable Energy Generation Sector*, 6 May 2013, DS412, 416. See F Ramírez Carmona, 'The Feed-in Tariffs Entanglement: A Comparative Study of the Analytical Approaches Followed by the EU and WTO Judiciary Bodies regarding Renewable Energy Subsidies' (2016) 43(2) *Legal Issues of Economic Integration*, 201.

47 See WTO, Appellate Body Report, *Canada – Certain Measures Affecting the Renewable Energy Generation Sector*, para. 5.147-5.191, in particular para. 5.185.

reliefs in favour of renewable energy may be found contrary to WTO law on subsidies.<sup>48</sup> The legal scholarship has criticised the Panel and Appellate Body, considering that they went “too far”, disregarding the ‘rule of the law’.<sup>49</sup> This argument – related to the idea that the Panel and Appellate Body promoted judicial activism - could be used as an additional argument to support the position that *ad hoc* legislation is needed in order to regulate energy policy, including energy tax reliefs.

From an EU perspective, the fact that WTO law does not seem to recognise similar environmental exemptions as under EU law could imply that energy tax reliefs – that are found compatible with EU State aid law – would however infringe WTO law surrounding subsidies. Both the EU and the Member States should therefore keep in mind the need that their energy tax reliefs comply not only with EU State aid law but also with WTO law.

#### IV. Conclusion: A Third Way - Need for *Ad Hoc* Legislation on Energy Taxation

This article highlights that neither EU nor WTO law play a useful role in guaranteeing that energy tax reliefs are based on environmental considerations. On the one hand, EU State aid law and WTO law surrounding subsidies are not helpful in prohibiting the adoption of polluting (fiscal) aid measures. On the other hand, EU State aid law and WTO law surrounding subsidies may put undue burden on Member States willing to adopt environmentally friendly energy tax reliefs.

Both EU law as well as WTO law seem to recognise the possibility for Member States to adopt ‘environmentally friendly’ energy tax reliefs. Nevertheless, Member States’ room for manoeuvre lacks legal certainty. Under EU law, regulations and guidelines provide some indications – however not always perfectly clear-cut - about the tax measures that can be found compatible with EU State aid law. Under WTO law, the room for manoeuvre of WTO Members is largely based on case-law and therefore also lacks legal certainty. Moreover, both the EU and the WTO could be blamed for legal and judicial activism given that the legal framework surrounding ‘environmental tax incentives’ is currently defined – at least indirectly - either by mere Commission’s regulations and guidelines or simply through WTO case-law. At the EU level, the decision to use regulations and guidelines surrounding State aid law to influence Member States in how they design their energy tax policy can be criticised in light of EU’s rules of competences. Indeed, harmonisation of tax matters at the EU level in principle requires the unanimity of the Member States and should not be indirectly adopted through Commission’s regulations or guidelines.<sup>50</sup> Finally, a last criticism regarding EU law concerns the fact that the legal framework established by the Commission does not guarantee that energy tax reliefs truly pursue an environmental goal.<sup>51</sup>

Overall, this article suggests that *ad hoc* legal instruments would better permit to regulate energy tax reliefs. Given the highly political character of energy issues, such new legal instruments are nevertheless unlikely to be adopted at the WTO law level (or at the level of any other international organisation,

48 A Genest, ‘Belgian and French biofuel support measures in light of Argentina’s challenge under the WTO Subsidies Agreement’ in Y Le Bouthillier, A Cowie, P Martin and Heather McLeod-Kilmurray, *The Law and Policy of Biofuels* (Edward Elgar 2016), 191 (assessing Argentina’s request for consultations regarding certain measures of the EU and the Member States in favour of biodiesel, WT/DS459/1).

49 For a critical analysis of this decision, see S Charnovitz and C Fischer, ‘Canada – Renewable Energy: Implications for WTO Law on Green and Not-So-Green Subsidies’ (2014) Discussion Paper Resources For the Future; L Rubini, ‘What does the recent WTO litigation on renewable energy subsidies tell us about methodology in legal analysis? The good, the bad, and the ugly’ (2014) 5 EU Working Papers Robert Schuman Centre for Advanced Studies, 3: ‘Everybody gives subsidies in support of energy. Nobody has an interest in raising a claim and risking a highly probable counter-claim. In other words, in what is certainly a simplified picture, the significant and spread subsidization in the energy sector has been tolerated until new factors came in and contributed to alter the equilibrium, in particular by making competitors’ subsidization harmful, waking up lobbies and special inter-

ests, and thus forcing governments to react”. See also P C Mavroidis, *The Regulation of International Trade, The WTO Agreements on Trade in Goods* (The MIT Press 2016), 221.

50 See Article 113 of the TFEU, Article 115 of the TFEU, Article 192 (2) (a) of the TFEU. A similar argument has been made by *Traversa/Flamini* (n 34) in the context of the fight against harmful tax competition, 330-331. See also A Haak and M Brüggemann, ‘Compatibility of Germany’s Renewable Energy Support Scheme with European State Aid Law – Recent Developments and Political Background’ (2016) 1 EStAL, 91, 100-101: “[C]ritics suggest that the Commission oversteps its competences in terms of energy policy explicitly laid out in Article 194 TFEU. However, nowadays the EU energy policy appears to be factually controlled by the Commission based on State aid rules”.

51 See J Englisch, ‘Energy taxation and key legal concepts in the EU State aid context: looking for a common understanding. Energy Tax Incentives and the GBER regime’ (2015) 51 CEU Serie Politica de la Competencia; N de Sadeleer, ‘State Aids and Environmental Protection: Time for Promoting the Polluter-Pays Principle’ (2012) 1 Nordisk miljörättslig tidskrift, 3.



such as the United Nations Framework Convention on Climate Change or the International Energy Agency). As for the EU, unsuccessful attempts to amend the ETD also illustrate the difficulties for

Member States to agree on common energy goals. This paper however shows that the use of State aid law cannot serve as a substitute to 'green' EU's energy tax policy.

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