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10-15-2022

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Recommended Citation

Hilsman, Sophia, "Inflation Reduction Act's Reception by Global Trading Partners" (2022). *CICLR Online*. 53.

<https://larc.cardozo.yu.edu/ciclr-online/53>

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Inflation Reduction Act's Reception by Global Trading Partners

By: Sophia Hilsman



The Biden Administration touted the Inflation Reduction Act (the “IRA”), signed on August 16, 2022, as “the most aggressive action on tackling the climate crisis in American history.”[1] The world desperately needs climate action. The seven warmest years recorded on Earth were 2015 to 2021.[2] In 2021, global fossil fuel carbon dioxide emissions “returned to the pre-pandemic levels of 2019.”[3]

There have been many attempts at international cooperation on climate change, including the 1992 Framework on Climate Change, the 1997 Kyoto Protocol, and the 2015 Paris Agreement.[4] In December 2015, 195 countries signed the Paris Agreement and agreed to combat climate change, peak emissions as soon as possible, and keep global temperature rise this century “well below 2 degrees Celsius” while “driv[ing] efforts to limit the temperature increase even further to 1.5 degrees Celsius above pre-industrial levels.”[5]

The largest contributor to global greenhouse gas emissions is the energy supply sector.[6] Transportation is another key sector. To achieve the Paris Agreement’s objectives, at least twenty percent of all road vehicles need to be electric by 2030.[7] Thus, major investment in zero-emission energy and vehicles is necessary to keep emissions below two degrees Celsius. Currently, the United States is very reliant on China for clean energy materials and components, such as lithium for batteries.

[8] The United States needs to establish new clean energy supply chains to become self-sufficient and meet climate targets. The Inflation Reduction Act is an important step towards necessary decarbonization.

The IRA invests \$370 billion into climate and clean energy over the next ten years.[9] One model finds the IRA's investments could help cut the United States' greenhouse gas emissions up to forty-three percent below 2005 levels by 2030, which is significant because the Paris Agreement's target is to cut emissions at least fifty percent by 2030.[10] The IRA uses tax incentives to achieve its objectives of creating American clean energy supply chains, manufacturing, and jobs.[11] This blog post [JP3] will highlight two areas of tax incentives that the IRA targets: energy and transportation. To spur demand, buyers of new electric vehicles ("EVs") can claim a \$7,500 tax credit or buyers of used EVs can claim \$4,000—if the vehicles meet the certain domestic production requirements.[12]

After August 16, 2022, to receive the clean vehicle tax credit, the vehicle must have been finally assembled in North America.[13] Starting in 2023, to receive the maximum tax credit, the vehicle's battery must meet certain sourcing, manufacturing, and assembly requirements.[14] For example, at least forty percent of the EV battery's critical minerals must have been sourced from the United States or a country with which the United States has a free trade agreement.[15] This percentage will increase over time, which could limit the number of qualifying vehicles in part because building new lithium mines for EV batteries could take years.[16]

The IRA's impact extends beyond the United States' borders. While many countries view President Biden signing the bill positively, as overdue action on climate, other trade partners are not happy with some of the protectionist provisions. Foreign automakers are impacted by the "Make it in America" provisions of the IRA.[17] For example, South Korea is concerned about the impact of excluding Korean-made EVs from consumer tax credits, and South Korea's Vice Foreign Minister met with the United States' Deputy Secretary of State to discuss "discriminatory elements" in the IRA.[18] South Korea, Japan, China, Germany, and the European Union have claimed that the IRA may violate international trade law and free trade agreements.[19] South Korea and other countries are reviewing whether to file a complaint with the World Trade Organization.[20]

The IRA ends tax credits for about seventy-two percent of previously eligible models, and according to Korea Automobile Manufacturers Association ("KAMA"), the policy could impact the export of 100,000 Korean EVs annually which are not assembled in North America.[21] KAMA claimed these tax provisions violate "the spirit of their alliance after Hyundai and Samsung announced U.S. investment plans totaling over 27 billion." [22] Of course automakers can decide to follow the incentives by moving manufacturing to the United States. Hyundai is already starting its construction of an EV and battery factory in Georgia ahead of schedule.[23] Similarly, for zero-emissions electricity, under the IRA there are certain tax credits available only for electricity made with products manufactured in the United States.[24]

Where does the World Trade Organization ("WTO") fit in? The WTO aims to remove any barriers to trade in member countries and unsurprisingly focuses on those aspects of a law over other policy goals. The relevant trade laws at issue are the General Agreement on Tariffs and Trade ("GATT") and the Agreement on Trade-Related Investment Measures ("TRIMs"). The national treatment principle, embodied under GATT's Article III, states that member states cannot discriminate against imported products once they have entered the market; instead, imported products must be "accorded treatment no less favorable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use." [25] The national treatment principle is also embodied in Article 2 of TRIMs.[26] Similarly, Article III, section 5 prohibits quantitative requirements, commonly known as "local content requirements" or "domestic content requirements" that require a "minimum threshold of goods, services, and/or labor [to be sourced] locally." [27]

Local content requirements help foster domestic industry and tend to reduce international competitiveness for similar goods. Despite this prohibition, they are regularly adopted.[28] Subsidies contingent on meeting local content requirements treat domestic and imported raw materials differently, which is prohibited by GATT and TRIMs.[29] There are certain exceptions including to protect "human, animal and plant life or health" as well as a government procurement exception.[30]

WTO violations can result in trade sanctions, which can have a chilling effect on environmental efforts to avoid the threat of WTO dispute or sanctions in the first place.[31]

Is the WTO going to stymie America's energy transition? Are the IRA's consumer tax credits tied to domestic source and production requirement violating WTO agreements? The EV domestic final assembly requirement and the sourcing requirements for batteries and clean energy industries appear to be the type of local content requirements that may violate the national treatment non-discrimination principle in GATT and TRIMs. However, reducing emissions and hastening our change toward a clean energy future is vital to meet the Paris Agreement targets. While nurturing domestic renewable energy and electric vehicle industries will admittedly benefit the United States, the policy is part of furthering broader environmental goals. Yet, the WTO has not often used the environmental exception in resolving disputes.[32] International agreements like the Paris Agreement, and local legislation to further climate goals, are at odds with the WTO's goal to promote free trade. Now is the time for diplomatic efforts to recognize the important environmental interests at stake before any complaint goes to the WTO, where the tax credits likely will be held to be inconsistent with GATT and TRIMs.

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- [1] See White House, *Fact Sheet: The Inflation Reduction Act Supports Workers and Families* (Aug. 19, 2022), <https://www.whitehouse.gov/briefing-room/statements-releases/2022/08/19/fact-sheet-the-inflation-reduction-act-supports-workers-and-families/> [<https://perma.cc/D6WD-3PTK>].
- [2] *United in Science 2022*, World Meteorological Org. 1, 4 (2022), https://library.wmo.int/doc_num.php?explnum_id=11308 [<https://perma.cc/VWN6-KNJF>].
- [3] *Id.* at 9.
- [4] Paul B. Lewis & Giovanni Coinu, *Climate Change, the Paris Agreement, and Subsidiarity*, 52 Univ. of Ill. Chi. L. Rev. 257, 262-63 (2019).
- [5] U.N. Climate Change Secretariat, *Contribution to the 2018 High Level Political Forum on Sustainable Development Submission from UN Climate Change* (2018) https://sustainabledevelopment.un.org/content/documents/18253UNFCCC_Contribution_2018_HLPF.pdf [<https://perma.cc/95BE-KK9Q>].
- [6] *Act Now: Facts and Figures*, U.N., <https://www.un.org/en/actnow/facts-and-figures> [<https://perma.cc/W8JD-S4NX>] (last visited Sept. 23, 2022).
- [7] *Electric Light Duty Vehicles*, U.N. Env't Programme, <https://www.unep.org/explore-topics/transport/what-we-do/electric-mobility/electric-light-duty-vehicles> [<https://perma.cc/Z3P3-D75A>] (last visited Sept. 23, 2022).
- [8] Jonah Nah, Joanna Lewis & Bentley Allen, *Can the U.S. Fight Climate Change – and Shift Industrial Policy?*, Wash. Post (Aug. 12, 2022, 7:45 AM), <https://www.washingtonpost.com/politics/2022/08/12/inflation-reduction-act-clean-energy/> [<https://perma.cc/5HKA-PFLF>].
- [9] Daniel Esposito, *Inflation Reduction Act Benefits: Clean Energy Tax Credits Could Double Deployment*, Forbes (Aug. 23, 2022, 7:15 AM), <https://www.forbes.com/sites/energyinnovation/2022/08/23/inflation-reduction-act-benefits-clean-energy-tax-credits-could-double-deployment/?sh=6b7d0b646727> [<https://perma.cc/6C6P-EHHV>].
- [10] *Id.*
- [11] See White House, *supra* note 1.
- [12] Inflation Reduction Act of 2022, Pub. L. No. 117-169, §§ 13401, 13402, 136 Stat. 1818, 1954-62 (2022).
- [13] Molly F. Sherlock, Cong. Rsch. Serv., IN11996, *Clean Vehicle Tax Credits in the Inflation Reduction Act of 2022* 2 (Aug. 24, 2022), <https://crsreports.congress.gov/product/pdf/IN/IN11996>.
- [14] *Id.*
- [15] *Id.* (explaining that additional restrictions for components sourced from any “foreign entity of concern” will begin in

- 2024).
- [16] *Id.*; see also Nah, Lewis & Allen, *supra* note 8.
- [17] See Yonhap, *S. Korea's Vice Foreign Minister Asks U.S. to Address 'Discriminatory' Part in New Law on Inflation*, Korea Herald (Sept. 16, 2022, 11:02 AM), https://www.koreaherald.com/view.php?ud=20220916000250&ACE_SEARCH=1 [<https://perma.cc/M556-8FRN>]; Joyce Lee & Heekyong Yang, *S. Korea Seeks Cooperation with EU over U.S. Inflation Reduction Act*, Reuters (Aug. 24, 2022, 11:07 PM), <https://www.reuters.com/business/skorea-seeks-cooperation-with-eu-over-us-inflation-reduction-act-2022-08-25/> [<https://perma.cc/N587-8S3X>].
- [18] Yonhap, *supra* note 17.
- [19] See Lee & Yang, *supra* note 17; *U.S. Trade Chief Tai Discusses EV Tax Breaks with Japan's Trade Minister – USTR*, Reuters (Sept. 9, 2022, 5:57 PM), <https://www.reuters.com/article/usa-trade-japan/u-s-trade-chief-tai-discusses-ev-tax-breaks-with-japans-trade-minister-ustr-idUSL1N30G2B6> [<https://perma.cc/97ZC-6RAY>]; *China Threatens Action Against 'Discriminatory' US EV Tax Breaks*, Bloomberg (Sept. 22, 2022, 5:33 AM), <https://www.bloomberg.com/news/articles/2022-09-22/china-threatens-action-against-discriminatory-us-ev-tax-breaks> [<https://perma.cc/SM89-QJHL>]; Jorge Valero & Jillian Deutsch, *EU is Assessing if U.S. Inflation Act in Breach of WTO Rules*, Bloomberg (Sept. 10, 2022, 8:26 AM), <https://www.bloomberg.com/news/articles/2022-09-10/eu-is-assessing-if-us-inflation-act-in-breach-of-wto-rules> [<https://perma.cc/95PL-967U>].
- [20] Lee & Yang, *supra* note 17.
- [21] *Id.*
- [22] *Id.*
- [23] *Id.*
- [24] White House, *supra* note 1.
- [25] General Agreement on Tariffs and Trade art. III, Oct. 30, 1947, 61 Stat. A-11, 55 U.N.T.S. 194 [hereinafter GATT].
- [26] Mukta Batra & Namit Bafna, *Renewable Energy: The WTO's Position on Local Content Requirements*, 39 Energy L. J. 401, 416 (2018).
- [27] *Id.* at 402.
- [28] *Id.*
- [29] *Id.* at 417.
- [30] *Id.* at 405-06.
- [31] *Id.* at 420.
- [32] Batra & Bafna, *supra* note 26, at 419-20.