



# Trade and Climate Change Briefing

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## BORDER CARBON ADJUSTMENT

Should countries be allowed to apply a penalty - in the form of a tariff or an obligation to purchase carbon credits - on imports from other countries that use less stringent emissions practices?

Opinions vary widely on this question, both within and outside the countries intending to apply such measures. But opinions are especially split within the global climate change negotiations, in which 192 nations are striving to find consensus on an international deal that is both effective and equitable. This issue promises to be particularly contentious in the final stretch of the Copenhagen meeting.

Known variably as border carbon adjustments (BCAs), border tax adjustments (BTAs), or border tax measures, (BTMs), it all boils down to the same thing: unilateral measures that a state imposes when a good is imported from an industry or firm in a country that has not 'comparably offset' the greenhouse gas emissions associated with the good's production. The BCA could be a flat tariff, a tax, or a requirement for the importer to purchase carbon credits that would compensate the country with more stringent regulations for the loss of competitiveness that it incurs because of its emissions standards.

Advocates of BCAs claim that the measures are intended to address three factors. First, competitiveness concerns where some industries in developed countries consider that a BCA will protect their global competitiveness vis-a-vis industries in countries that do not apply the same requirements. The second argument for BCAs is 'carbon leakage' - the notion that emissions might move to countries where rules are less stringent. A third argument, of the highest political relevance, has to do with 'leveraging' the participation of developing countries in binding mitigation schemes or to adopt comparable measures to offset emissions by their own industries.

Indeed, from a political perspective, both experts and politicians argue that it may be impossible for

some countries, notably the US, to take strong climate action in the absence of BCAs.

BCAs could, in theory, be applicable to any importing country. In practice, however, they would initially be directed at developing countries, and would be primarily aimed at exports of those industries that exceed a certain threshold of global emissions, or that account for more than a certain percentage of the BCA-imposing country's imports of the good in question.

The United Nations Framework Convention on Climate Change (UNFCCC) differentiates between the global responsibilities of developed and developing countries regarding mitigation. Currently, the Kyoto Protocol only binds developed countries to emissions reduction targets. A future global agreement will also most likely differentiate between developed and developing countries on the basis of their "common but differentiated responsibilities and respective capabilities," as laid out in the UNFCCC, taking into consideration the historic responsibility of developed countries whose industrial development precipitated the current climate crisis.

### Developing countries oppose the measures

Proponents also argue that BCAs would motivate developing countries to increase their mitigation action. However, from a developing country perspective, at least three arguments run counter to that idea: 1) that the use of BCAs is a prima facie violation of the spirit and letter of multilateral trade principles and norms that require equal treatment among equal goods; 2) that BCAs are a disguised form of protectionism; and 3) that BCAs undermine in practice the principle of common but differentiated responsibilities.

The issue has sparked heated discussions in the context of the global climate negotiations and will likely be a point of contention through negotiations at the Conference of the Parties (COP) in Copenhagen this December. The issue arises in two sections of the current draft negotiation text

for a new climate deal. At a negotiating session in June, India and China, supported by dozens of developing countries, introduced language in two areas of the draft text to prevent the use of such measures. The current text reads as follows:

“Developed country Parties shall not resort to any form of unilateral measures including countervailing border measures, against goods and services imported from developing countries on grounds of protection and stabilization of the climate. Such unilateral measures would violate the principles and provisions of the Convention, including, in particular, those related to the principle of common but differentiated responsibilities (Article 3, Paragraph 1); trade and climate change (Article 3 paragraph 5); and the relationship between mitigation actions of developing countries and provision of financial resources and technology by developed country Parties (Article 4, Paragraphs 3 and 7).”

The BCA paragraph has received most discussion under the informal group on ‘economic and social consequences of response measures’ - one of six mitigation sub-categories under the Bali Action Plan. This sub-section is intended to consider and include provisions that would abate the impacts arising from actions taken by countries to mitigate climate change. The BCA paragraph was also introduced into the draft section on ‘a shared vision,’ which is the introductory section of the draft text. This section contains principles and goals for the new agreement and reflects the tone and approach of the entire text. Since initial discussions at the introduction of the paragraphs, they have not been altered or received substantial further discussion, thus leaving their consideration to Copenhagen.

### **BCAs in US climate legislation**

Language on BCAs - both in favour and opposed - appeared in the global climate negotiating text shortly after the US House of Representatives approved draft climate legislation in June (see Bridges Trade BioRes, 26 June 2009, <http://ictsd.org/i/news/biores/49571/>). Despite some internal controversy, the issue has survived into the Senate version of the proposed legislation, known colloquially as the Boxer-Kerry Bill, where it is currently under consideration. If passed in the Senate and approved by the president, the bill will become law and the details on institutions and implementation of the BCAs will be hammered out in an internal Senate Committee.

Despite some uncertainty as to whether the US legislation will successfully run its course, the bill now on the table has significant bipartisan backing. In a recent New York Times op-ed by Democratic Senator John Kerry and Republican Senator Lindsey Graham, the two lawmakers expressed their confidence that the legislation will pass. Notably, the senators also said that the climate legislation will have to include a BCA provision if it is to win lawmakers’ approval.[i]

“We cannot sacrifice another job to competitors overseas,” the senators wrote. “China and India are among the many countries investing heavily in clean-energy technologies that will produce millions of jobs. There is no reason we should surrender our marketplace to countries that do not accept environmental standards. For this reason, we should consider a border tax on items produced in countries that avoid these standards. This is consistent with our obligations under the World Trade Organization and creates strong incentives for other countries to adopt tough environmental protections.”

But US President Barack Obama has on numerous occasions criticised the use of BCA. “At a time when the economy worldwide is still deep in recession and we’ve seen a significant drop in global trade, I think we have to be very careful about sending any protectionist signals out there,” Obama said in Washington in June. He has also noted that the draft legislation already included various other kinds of transitional assistance for energy-intensive industries even before the border tax adjustment provisions were reinserted, and he has underlined the importance of maintaining a level playing field internationally.

In Europe, France’s President Nicolas Sarkozy has been promoting BCAs since France crafted its own draft legislation last September. Yet, despite strong criticism from European Union’s Environment Commissioner, Stavros Dimas, members of the French delegation at the climate meetings claim the country is currently working to extend the legislation to the entire European Union with some success. A number of EU member states have reportedly indicated that they would look on such an option favourably.

Apart from being a controversial issue for political reasons, analysts have long expressed doubts both regarding the efficacy of such measures with regards to leakage concerns and their compatibility with WTO-rules. Moreover, the administrative

exercise that would be necessary in order to calculate carbon contents is considered to be near to insurmountable. On top of this are the political costs: trying to impose environmental considerations on countries through tariffs risk creating bad will in the negotiations on climate change, in the trade negotiations of the DDA and in the multilateral trading system. As stated by China's Minister Cheng in response to the language approved in June in the House, it will likely trigger retaliatory action, in the worst case leading to a trade war. Costs could be considerable both in terms of economics and environment

The issue of BCAs will likely remain on the table until late in the negotiations in Copenhagen. Yet the clear conflict with US forthcoming legislation casts a shadow of doubt over whether it will appear, as formulated, in the final agreement. Considering the complexity and political sensitivity of the issue, there may be need to craft some place-holding language for Copenhagen and continue negotiations on the topic into the future - a fate that is likely to be shared by many issues that cannot be readily solved in Denmark this December.

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