

The feasibility of a European carbon border adjustment mechanism

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PRESENTATION

Confrontations Europe and the College of Europe co-publish this article on the feasibility of a European carbon border adjustment mechanism, written by David Radji and Alexis Gourdain, two recent College of Europe graduates.

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The next level of a global European Union (EU) strategy to fight Climate change and create a level playing field is the introduction of a global framework to control and penalize the excess of CO2 emitted during the different phases of production of goods entering Europe(1). This proposal was part of the President of the European Commission's main proposals for the European Green deal, Ursula Von der Leyen, in her candidate speech to the European Parliament. With the impact assessment and consultation already completed, the Commission's formal proposals is awaited by late June 2021. An own-initiative report titled "Towards a WTO-compatible EU carbon border adjustment mechanism" (CBAM), negotiated by the French MEP Yanick Jadot, was recently adopted by the European Parliament. Rather than actively taking side for one specific design of CBAM, the report assesses all the various shapes the mechanism could take over institutional, trade-related and own resources issues.

The idea of implementing such a mechanism did not come out of the blue. Indeed, the debate already started more than 20 years ago, with the signature of the Kyoto Protocol, when it was decided to cut GHG by at least 5% (in committed countries), from 1990 levels, during the 2008-2012 commitment period. It was this Protocol which first gave rise to the idea of an Emission Trading System, of which the EU has been quite skeptical. Indeed, the

concept of environmental taxation has been a harsh debate within the EU, as the outcomes of putting a value or a price for free common goods in order to safeguard them in distributing the cost of their use and pollution was never tried before at such a vast geographical scope.

However, in the wake of Kyoto, the European Commission decided to spearhead this ambition and to prepare the launch of its European-wide Emission Trading System (ETS). This 'cap-and-trade' system is an instrument based on the distribution and exchange of carbon emissions allowances or permits (in tons of CO2) to industry that represents around 45% of the global EU emissions' framework. Pursuant to Pigou's concepts of environmental externalities and advocated by Christian de Perthuis(2), the goal of this system is to use the market's principles (supply and demand on allowances) to orientate carbon pricing and bolster low-carbon emitting innovation in industries covered by the system. By putting a price on carbon, carbon markets encourage those industries to reduce their emissions and then selling their spared carbon allowances and/or avoid hypothetical penalties if they overtake their emissions' allowances. This system ended up being increasingly criticized for its lack of ambition and endogenous functioning issues. The debate is still open amongst economists concerning its efficiency in mitigating climate change, as for the time being its price signal has remained low(3).



Simultaneously, the idea of a carbon border adjustment mechanism was discussed several times to complete the objectives of the EU ETS. Indeed, the system was created and developed in an attempt to consider some problems that may occur such as carbon leaking, low carbon prices and level-playing field issues such as loss of competitiveness for ETS-covered sectors. However, it did not spur the expected worldwide enthusiasm (also conceptualized as the *Brussels effect*(4)), which would have created a global Emission Trading System stemming from the gradual development of regional ETS system across the world. Indeed, although California and China(5) decided to implement their own system too, the attempt to reduce the worldwide CO₂ emission through ETS has not been achieved yet. That is why three “adjustment” proposals have been debated at the European level since 2007, each of them in the frame of EU ETS revision. In 2005 the first stage of the European ETS was launched and was later revised in 2007 and in 2013. The fourth phase is expected to be released in 2021. In the frame of the 2007 revision, the concerns of highly emitting industries, such as cement, grew regarding hypothetical loss of competitiveness and carbon leakage. Indeed, the reform included the move from the free emission permits system to an auction system, which was interpreted as a one-way effort for EU industries and the absence of a level-playing field. Following this period, there was a growing desire for

a global scheme, allowing a level-playing field along with a completion of Climate goals. De facto, the third phase (2013-2020) was meant to include, “pertinent sectors’ imports in the EU ETS”(6), although this has remained an informal proposal of the European Commission, and to create remuneration for exporting industries so to solve the competitiveness issue. This was eventually discarded in favor of the scheme of free allocation for the industries most exposed to international competition. After this attempt, the European Commission has not yet tried again to pursue the path of an adjustment mechanism. However, France did not give up and reintroduced this idea twice. The first time in 2009 for the third phase revision where it proposed a “carbon inclusion” mechanism to oblige importing industries to buy emissions permits under the EU ETS. The non-paper encompassed criteria to ensure the compliance with WTO rules, revised the scope of the mechanism so to encourage reluctant countries to enter negotiation on a global climate agreement and targeted only the production-related emissions. The European Commission did not follow up the initiative with a formal legislative proposal. After signing the Paris Agreement, France issued a new proposal specifically targeting the cement industry in February 2016. It aimed to substitute free allowances previously granted to European cement industries with a similar emission mechanism for cement importers. Although the proposal found its way through the ENVI committee of the European

Parliament in the frame of the fourth phase's revision of EU ETS (2021-2030), it was eventually rejected in plenary session as free allowances were once again favoured by MEPs. The rationales for this rejection were based on the lack of legal basis pursuant to WTO rules compliance and the risk for measures to be perceived as a hidden type of economic protectionism.

But today, the paradigm has changed. When asked why such a measure could be implemented today, while constantly rejected in the past, Clement Beaune, French Secretary of State for EU Affairs, answered that "Climate urgency has been taken more seriously by the European Commission than ever before, and the need to ensure our competitiveness in the wake of the Green deal has also helped". He added, "Five or six years ago, we were standing alone. Today, there are at least 15 Member States ready to bargain on the implementation of a CBAM"(7).

De facto, although there is some certainty about the fact that such a proposal will be tabled by the Commission, questions remain on how and to what extent? This paper attempts to answer both issues, focusing on technical reviews and last released information on three points: (I) the technical challenges; (II) the international pressures; (III) the current political situation in the EU institutions. Before developing the different proposals and discussing the underlying issues of an EU

carbon adjustment mechanism. We must emphasise that each part will develop specifically the most suitable solution to adapt this new scheme to various overlapping obstacles: EU ETS extension.

I. Implementation and technicalities: which frame for an EU adjustment mechanism?

Before developing the diplomatic and political challenges of the EU ETS, the institutional, technical and administrative obstacles must be discussed in order to outline the best suitable framework for a European carbon adjustment mechanism.

An adjustment mechanism would aim at "placing carbon price on imports of certain goods from outside the EU"(8). The problem is that there are a myriad of ways to achieve this goal. Three main possibilities could thus be numbered: excise duty/tax on consumption, custom duty/tax on imports or based on the EU ETS as an extension of it. The first two are based on price and the last one on quantities. Each of these three options has different consequences and none of them are entirely perfect.

First, a tax on consumption will be highly difficult to implement for political reasons. Bearing in mind the consequences in France of the diesel car taxation and the subsequent yellow vest crisis, tax on consumption does not appear as the best solution to fairly split the costs and benefits of the mechanism. It is also quite complex

technically as all EU populations do not have access to the same technologies and their current situations do not allow harmonized taxation. The example of cars is quite revealing on this point. Indeed, taxation on diesel-driven vehicles would be far more harmful for Eastern populations than for Western ones⁽⁹⁾. Indeed, the latter benefit from better transport infrastructures across their territory that allow a fair share of their citizens to abandon cars for public transportations. It is not the case in most Eastern countries where the average motorization rate is higher than in the West⁽¹⁰⁾. Furthermore, for equal weight vehicles, Western citizens can afford less-emitting cars than Eastern citizens⁽¹¹⁾. Those issues make the idea of harmonized taxation complex to calculate at EU-level. Besides, the institutional viewpoint would require unanimity in the Council, which is necessary for fiscal matters. It goes without saying that such an unanimous perspective on European taxation cannot be imagined in the near future⁽¹²⁾.

The custom options would be a deliberate attempt at implementing protectionist policies, which is forbidden by WTO rules and thus cannot be seen as a relevant option. We will develop this point later on.

The last option, which is probably the most viable in several ways is an extension of the Emission Trading System. Firstly, from the institutional and implementation viewpoint, it would ensure – from a

theoretical perspective – a swift decision-making process, as only qualified majority is required in the Council. Furthermore, the ETS is core to EU strategy against Climate change from 2005 onwards. However, some issues still loom on the adjustment mechanism's viability in an ETS design. First of all, would such a mechanism be linked to ETS in all regards, especially to the scope of application? How would carbon pricing be calculated? Would raw materials extraction be considered as part of the emitting framework, or only the production phases? What geographical area should be covered if we consider the issue of developing countries that mostly welcome foreign industries and have little leverage on the way they produce? Should they be helped as Yannick Jadot stated in its own-initiative report?

First, the scope of the mechanism will be essential in the discussions. In theory, the scope of the adjustment mechanism would cover all imported products throughout the whole value chain, bolstering its capacity to prevent carbon leakage and enforce the level playing field in favour of EU economies. Yet, in practice, the technical complexity and administrative cost of such a large covering for imported goods — specifically for complex manufactured products — would be highly disproportionate to the pain/gain ratio of such a mechanism⁽¹³⁾. In fact, this issue is strongly linked to the way in which carbon pricing will be calculated. Indeed, we recall that the adjustment mechanism requires



globally comparable data, for example comparable production processes worldwide, in order to objectively calculate the level of pollution and set a price for imported goods. By the price of imported goods, we mean the number of allowances that must be purchased to allow the goods to enter the EU market. It is indeed easier to calculate the greenhouse gas emission of a certain production because it is quite standardized at the global level, while such a price could be more difficult to assess for other productions, such as cars, because the production process can vary considerably from one model to another(14). Some researchers even advocated for such a limited scope, specifically the EITE (Energy-Intensive and Trade-Exposed sectors) as it would decrease administrative and technical costs and administrative burdens of such a mechanism while “still delivering significant environmental benefits”(15). An attempt to further broaden the scope would greatly complicate the determination of the “right price” to achieve the cut in emissions needed without over or under-charging companies. The issue of the EU ETS’ scope enlargement shall then be raised : if the adjustment mechanism is to be linked to the EU ETS, to what extent will it follow its revisions in the future? Today, the adjustment mechanism seems to be only possible, when considering high-emitting industries such as cement, steel and aluminum, “where the value of embodied carbon products, as a percentage of value added, tends to be relatively high

compared with manufactured products”(16) — while discussions about the fourth phase of the EU ETS emphasise an extension of its scope.

Second, the number of allowances authorized at the global level would also be regulated by the Commission or a related independent institution, which consequently constitutes an extra-administrative layer that will weigh on an already complex framework. Decisions shall be made over allowances’ sources for importers. The ERCST Research Group outlined two possibilities: either allowances are removed from the existing allowance pool such as the Market Reserve Stability, and allocated to importers, or another fresh allowance pool is created. However, both solutions can entail negative consequences. The former would send a strong price signal and increase the price of carbon as investors would notice the Commission’s intentions to firmly reduce the hypothetical future release (as the Market Stability Reserve would lose part of its saved allowances). At the moment, the consequences of the latter are merely speculative as, depending on the amount released by the Commission, the price could vary exponentially. Nevertheless, bridging the adjustment mechanism and the EU ETS would eventually add a layer of administrative and technical difficulty to the system.

Third, calculation and decisions shall also be made on the emissions scope of the adjustment mechanism, e.g. which stages



of production are considered to calculate the amount of emissions of imported goods. Emissions are to be classified in three categories according to the Western Research Institute: direct for those stemming from the production itself, including emissions linked to energy consumed (use of electricity and/or combustion of fuels); indirect for emissions related to those emitted offsite or arising during the lifecycle of the imported goods... and all other indirect emissions. Depending on the way emissions scope will be calculated, foreign business could even “develop ways to circumvent the tax”, hence the need to be vigilant⁽¹⁷⁾ and target specific sectors on which we can easily enforce calculation and controls. If we rely on the scheme we have been developing in this paper, meaning bridging EU ETS and adjustment mechanism, we should note that the former only cover direct emissions from industry, aviation and the power sector. Administrative coherence would thus advocate for symmetric design against climate and environmental ambitions. Indeed, ‘adjustment’ has a clear sense of pasting the rules applied domestically to another level. Therefore, if we want to raise the bar, we need to raise it in the EU ETS, in order to enforce the notion of level-playing field and elevate the domestic rules to the international-level. It goes without saying that, although criticized for its lack of ambitions and its limited scope, any extension of the EU ETS would induce further administrative burden to ensure the calculation and good

administration of such new rules. An asymmetric scheme between EU ETS and the adjustment mechanism could also be developed but would clearly raise the issue of distortion in the market with some products being covered by the EU ETS and not by the CBAM and vice versa. Goods that are not covered would then have a clear advantage over those falling under the scope of one of those two regulations, which would distort the market. In this regard, some specific custom regimes should be abolished so to avoid encouraging long-value chain products through European custom preferences, and others developed so to circumvent loss of competitiveness for EU companies as side effect. For instance, an outward-processing procedure is a highly polluting process, which allows a product of EU origin to be processed in a third country duty-free and then re-imported for sale in the EU. These rules shall be refitted in order to comply with the CBAM objectives. Also, from a pure competitiveness-related point of view, we shall discuss how different products will be covered, depending on their use in the value chain. For instance, in case of long-value chain — although it must be avoided —, European companies could suffer from the higher prices of intermediary goods due to CBAM, which will eventually impact the price of the final good⁽¹⁸⁾. On the contrary, following the same observation, foreign goods will be advantaged as long as no CBAM will be implemented at the borders of their production place. From an EU perspective, we may assume that it is not a

big deal, as these foreign goods will be affected by the CBAM as soon as they enter the single market. However, from a global perspective, the EU products will just reflect a higher price and will thus be disadvantaged when it comes to exporting. An export subsidy scheme should thus be created to allow EU producers to access the global market, despite the breach it could create with the WTO rules.

II. A protectionist or pioneering Europe? The international challenges of implementing the CBAM

In addition to the technical and administrative complexity of implementing a carbon border adjustment mechanism, the European Union also faces challenges coming from the international level. Indeed, in an open economic market, it is impossible for the EU to implement such a mechanism alone, without considering the rules of the World Trade Organisation and without consulting its trade partners. Despite these challenges, the implementation of the CBAM could also be a way for the EU to export its environmental and climate standards, the Green deal enabling a normative soft power, and to bring the other countries into the team by adapting a similar mechanism.

2.1. 'Towards a WTO-compatible mechanism

Creating a WTO-compatible CBAM is one of the main challenges of EU institutions, hence the name of the report

discussed in the EP: 'Towards a WTO-compatible EU carbon border adjustment mechanism'(19). Indeed, both the European Union and the Member States are parties to the World Trade Organisation. They are bound by international law and must ensure WTO rules. Even though the agreements cannot have a direct effect in the EU Court of Justice, other WTO members can take the EU into a state-to-state dispute settlement, hence the necessity to respect these rules. Moreover, as most WTO rules date back to the 1940s -- when the General Agreement on Tariff and Trade (GATT) was concluded -- there are no rules addressing climate change. In their article, Mehling and Ritz(20) lay out concerns raised by the WTO based on the potentially discriminatory nature of the CBAM.

When reading the EP report and the paper published by the Delors Institute(21), three main GATT articles must be taken into consideration when designing the CBAM to avoid protectionism; they refer to internal and external discrimination, favourable treatment and environmental exceptions. The CBAM first challenges the GATT Article(22). on General Most-Favoured-Nation Treatment which prohibits measures which have the effect of allowing differential commercial treatment to imported goods of different origins, but which are considered similar. The mechanism also challenges the GATT Article III prohibiting regulatory and fiscal discrimination between imports and domestic products, but also authorising the imposition of a border tax corresponding to

domestic tax levied on certain products. This means that it is not possible to impose a differentiated direct or indirect charge between equivalent imported products; imports should not favour domestic production.

Moreover, even though GATT Article II (1)) prohibits the unilateral implementation of less favourable trading conditions by a party, Article II (2)(23) stipulates however that “nothing in this Article shall prevent a contracting party from imposing at any time, on the importation of any product, a charge equivalent to an internal tax imposed consistently with the provisions of paragraph 2 of Article III*, in respect of the like domestic product or in respect of an article from which the imported product has been manufactured or produced in whole or in part”. According to Lamy et al., this article should indeed be taken into consideration in case the CBAM is considered as “a customs duty calibrated to the average carbon intensity of European industries and the domestic price per tonne of CO₂”(24).

Despite previous articles, the CBAM could find its legal basis in GATT Article XX(25) which grants, in paragraph b) an exception for measures “necessary for the protection of human, animal or plant life or health” and those “necessary for the conservation of exhaustible natural resources” in paragraph g). Carbon leakage could thus fit into this exception. However, such measures should not “constitute a means

of arbitrary or unjustifiable discrimination between countries”. The CBAM should thus be as transparent and predictable as possible to fit into WTO rules so that the EU could avoid potential disputes.

While WTO legality is essential for CBAM to succeed, the EU could also choose to violate WTO rules since the remedy precludes monetary compensation, so that in a worst-case scenario the EU would be forced to adapt the mechanism or face an equivalent trade counterattack(26). This decision would send a protectionist image of the EU, which it wants to avoid as much as possible.

As written before and proposed by the French Renew MEP Canfin(27), the best option to remain in the WTO legal framework would be to mirror the EU ETS. In Lamy et al., authors explain that “an indexation of the import quota price per tonne to the domestic price per tonne in the EU ETS the day before the product enters the territory of the European Union would also provide indispensable guarantees of non-discrimination vis-à-vis domestic production under GATT Article III.”(28).

2.2 An increasing international pressure

The difficulty of designing a WTO-compatible mechanism is closely linked to diplomatic and trade relations. Since the announcement of setting up a CBAM, the EU is facing pressures coming from its main trade partners such as China. The

Chinese government has already expressed its reluctance to implement a European carbon border mechanism, as it fears having new customs duties imposed on it. The CBAM could be seen as a unilateral decision from the EU, with clear consequences and costs for the rest of the world. China said that “more consultation is needed”(29) to design a mechanism that does not impede international trade. On the Asian continent, China is not the only country expressing doubts about the CBAM. In a recent survey published by the Konrad Adenauer Foundation(30), eight countries (Australia, China, India, Indonesia, Japan, Singapore, South Korea, and Thailand) have a somewhat negative perception of the European initiative. India considers it as “protectionist, discriminatory towards developing countries, and contrary to international laws and agreements”. If unsatisfied, these countries could take action at the WTO level.

On the other side of the Atlantic, the election of Joe Biden will most likely lead to changes, as the US is now, unsurprisingly, closer to the EU's climate strategy. Indeed, unlike former US President Donald Trump who seemed reluctant to implement such a mechanism, the topic is set in the 2021 Trade Agenda of the Biden administration and is trade priority(31). President Joe Biden could even use the same strategy as his predecessor and unilaterally implement the carbon border mechanism based on national security risks. Such an implementation could revive trade tensions.

If some countries consider the CBAM a protectionist tool, this is not the EU's perception. In an article published in Le Monde, former WTO DG Pascal Lamy argues that “Covid-19 will accelerate the shift from protectionism to precaution”. This is indeed the case with the acceleration of the debate on the implementation of a CBAM. According to Pascal Lamy, “it is no longer companies that need to be protected with tariffs against international competition, but citizens and consumers who need to be protected against various risks”(32). This spirit can be found in the European Green deal proposed by the European Commission, and in President Von der Leyen's will to develop a 'geopolitical Commission'. The implementation of the Green Deal will allow the EU to continue exporting its environmental standards internationally and to gain influence on the climate issue, making the Union a market and normative power. The EU is already seen as a forerunner in this field. China recently set up a national carbon emissions trading system on the advice of the European Commission(33). This example shows how the EU serves as a model in this field and it could be an example of the “Brussels effect” and the idea of “race to the top”. If China is now reluctant to set up a CBAM, it may change its perspective once the EU or the US has set up their own mechanism. According to Secretary of State Clément Beaune, the idea is “not to allow a form of dumping to be re-imported into our European market”(34).

Finally, the diplomatic and trade issues we just discussed are closely linked to the CBAM's geographical scope. Indeed, while some developed countries can afford to accelerate their green transition, others, lacking technological means and production methods, will be penalized by the implementation of CBAM even though they pollute much less. Should they also pay? The geographical scope is also closely linked to which economic sector should be impacted. The Commission said it was likely to experiment with the CBAM with industrial sectors such as steel and cement, which does not satisfy some countries like China.

To solve these issues and ease the potential growing tensions with trade partners, a lot of ideas have emerged. First, one should examine former French finance minister Edmond Alphandéry's idea⁽³⁵⁾ of creating a global carbon price for the three main emitters: the US, China and the EU. This would allow the EU to avoid the deterioration of diplomatic relations as well as the undermining of global efforts to fight climate change. Moreover, French Renew MEP Pascal Canfin advocated that the implementation of the CBAM and the free allowances, which are currently in place in the framework of EU ETS, would not be WTO-compatible, creating a "dual protection"⁽³⁶⁾. Indeed, free allowances could be equivalent to subsidies in WTO rules and lead to trade distortion as we saw previously.

III. The state of the debate within European Institutions, the hardest is yet to come

3.1 A global agreement between Member States to discuss the matter, but the devil is on the details

In the global summary stating the positions of France in the frame of the Portuguese Presidency, the Secretariat General for European Affairs wrote that "France supports the implementation of a WTO-compliant Carbon border adjustment mechanisms"⁽³⁷⁾ and added that "Poland, Hungary, Czechia, Lithuania, Italy and Spain supported the introduction of such a mechanism with France". On a common letter addressed to the European Commission, a group of Member States including Austria, Denmark, France, Luxembourg, Spain, Slovakia and the Netherlands advocated for a CBAM "proposal by 2023 that is effective, legitimate and fair": "Effective, because it can tackle carbon leakage better than existing instruments. Legitimate, because it will be in full compliance with the international rules laid down by the World Trade Organization and consistent with the framework of the Paris Agreement. And fair, because it will be implemented in a transparent and coordinated manner with our trading partners, without discriminating between domestic and foreign producers". Although the wording is soft, we can easily see that a large coalition is being built around France that amounts to more than 10 countries, as Clement Beaune⁽³⁸⁾. Even Germany is open to discussion, whereas it



was opposed to it at the end of 2020, as its Minister of agriculture stated: we need to “ensure that climate action in the bloc’s farming sector doesn’t endanger farmers’ livelihoods and cause carbon leakage”(39).

The principle is then not a problem for the Member States, but it will surely become one once the technical details will be touched upon such as the scope of the mechanism. Clément Beaune was clear when developing the French position, admitting that “we are not capable to include all sectors in the EU ETS, that is why we shall focus on high-emitting sectors such as cement and steel for measurement of carbon price easier than for other sectors as production process is quite standardized worldwide”. Conversely, Poland advocates for the inclusion of fertilizer in the scope of the mechanism, which would go against the principle of symmetry with EU ETS, as discussed before, and would make coherence of the CBAM even more difficult to justify. The same can be said for Germany, which seems to support the inclusion of the farming sector in the adjustment mechanism. With the European Parliament being divided, we shall expect the same from Member States. For now, no agreement can be ascertained, but it is likely that the common interinstitutional denominator will be the cement and steel industries, thus entering the French expectations’ framework. However, this situation will take from the European Parliament to accept the removal of free

allocations for certain sectors, which it refused by a narrow margin in March 2021 for competitiveness concerns(40).

3.2 A lively debate within the European Parliament: the issue of free quotas

At the EP level, debates are very lively between the different political groups. On March 10, 2021, French Green MEP Yannick Jadot presented his report ‘a WTO-compatible EU carbon border adjustment mechanism.’ The report introduced several answers to the issues we raised throughout this paper. For instance, it advocates granting special treatment for less-developed countries and small islands – Jadot goes further asking the CBAM to finance the green transition in these countries(41). Moreover, regarding the scope, the report stipulates that “CBAM should cover the power sector and energy-intensive industrial sectors like cement, steel, aluminium, oil refinery, paper, glass, chemicals and fertilisers, which continue to receive substantial free allocations”(42).

Finally, it deals mainly with WTO compatibility and provides an answer to the questions raised above.

During the presentation of the report in the EP plenary session, the debate crystallised around a key element, the phasing out of free allowances and this specific sentence at point 28 of the report(43) : “emphasises that the implementation of the CBAM should therefore go hand in hand with the parallel, gradual, rapid and eventual

complete phasing out of those measures for the sectors concerned so as to avoid double protection for EU installations.”. During his intervention, the Polish EPP MEP Adam Jarubas declared that “the possible phasing out of free quotas could have a detrimental effect on European exporters. If we eliminate them, we could encourage carbon leakage not in the sectors directly concerned, but in those that depend on their production”(44), supporting the idea that CBAM cannot be an alternative to free quotas. This created a shift within the EPP political group as French EPP MEPs, from Les Républicains, decided to side with French Greens and French Renew MEPs. The creation of the CBAM is to be found in the manifesto of Les Républicains MEPs for the European elections and the mechanism was an idea already proposed by President Sarkozy in 2008(45).

In the final report adopted by the EP, the amendment deleting the phase out of free allowances passed. It seems that a front of Conservative MEPs is being created against a front of “green” MEPs coming from Western countries. An article published in Politico(46) reveals that big industry groups, especially those representing steel, chemicals and cement sectors, lobbied in favour of keeping free allowances, using the argument of the loss of competitiveness when exporting their products. As explained above, maintaining both systems in place could result in action at WTO. During the debate in the EP,

Commissioner Gentiloni recalled that the CBAM must respect WTO rules. Moreover, former WTO DG Pascal Lamy deplores the deletion of the phase out in the final report, tweeting that it “sent a very bad signal (...) definitively putting CBAM under threat at WTO”(47).

Conclusion

This paper discussed the feasibility of designing a Carbon border adjustment mechanism at EU level. We noticed throughout the paper that the design encounters several obstacles from technical to administrative, passing by international law and pressures, as well as intense debates within European institutions. Technical and administrative challenges are probably the most important, which is why the CBAM should be modelled on the EU ETS in order to gain consistency and feasibility, both in terms of technical feasibility and compatibility with WTO rules, as Pascal Lamy has argued. We have seen that WTO compatibility is the main debate at the international level, but also within the European institutions, on the grounds that free quotas could create double protection, if they remain in place with CBAM. Moreover, international carbon pricing will enforce the high environmental standards of the EU worldwide and at the same time tackle carbon leakage.

Finally, we can conclude by saying that the old French idea of a CBAM will finally see the light of day. The Covid-19 crisis has



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accelerated this debate and the setting up of the mechanism. As the EU has decided to go into debt in order to finance the Recovery plan NGEU, implementing new own resources, especially since Brexit, has become essential. According to the EP own-initiative report, the mechanism should bring between 5 and 14 billion euros per year, which should allow the Commission to finance the green transition. The Commission must now present a legislative proposal in the second quarter of 2021 and the mechanism must be operational by 1 January 2023, according to the new own resources directive. The own-initiative report of the EP already gives us a hint of the main issues at stake. To quote the rapporteur Yannick Jadot, “the battle has only just begun”.

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