



15 June 2010

### **CLIMATE CHANGE, TRADE AND COMPETITIVENESS: ISSUES FOR THE WTO**

#### **ROUND TABLE III: CLIMATE-LINKED TARIFFS AND SUBSIDIES: ECO-LEGAL INTERFACE**

Speaking notes for Carsten Dannöhl, Senior Adviser, BUSINESSEUROPE  
16 June, TAIT Trade and Climate Conference, Geneva

Ladies and Gentlemen,

I would like to thank very much the organizers for having invited me and giving me this opportunity to present our views. The issue we are discussing today – the link between trade and climate change – is of particular importance to European companies. I would like to thank Patrick Low, Gabrielle Marceau and Julia Reinaud for their very interesting background paper. This paper clearly lays out a number of open questions in the discussions on carbon border adjustment measures.

Just a few words about BUSINESSEUROPE before entering into the theme of this panel: our organization has been the voice of European companies vis-à-vis the European institutions for more than fifty years. BUSINESSEUROPE brings together 40 industry and employer federations from 34 countries as well as 37 associate member companies. Our main objective is to promote the interests of European companies with a particular focus on policies and rules that could influence their competitiveness. Promoting open trade, fighting protectionism and tackling climate change are among our key priorities. An important element of this strategy is working towards the conclusion of a comprehensive international climate change agreement. Climate change can only be tackled globally. However, the international climate conference in Copenhagen was a disappointment.

With the absence of an agreement, the use of border adjustment measures is being brought up by politicians and stakeholders. This has been done in reaction to existing and emerging regional climate policy disparities and resulting negative effects on national economies and sectors of countries with stringent commitments and constraints. However, the threats of unilateral border measures have been counterproductive to finding a multilateral solution and have not motivated skeptical countries to commit to emission reductions in Copenhagen.

The principal justification for border measures is the phenomenon of “carbon leakage”. To many European politicians, border measures appear to entail a win-win situation to confront this question: both the climate and the competitiveness of the domestic industry are protected. BUSINESSEUROPE does not share this opinion. From our



point of view, border adjustment measures neither serve an environmental nor an economic objective. In addition, they would add a layer of legal uncertainty which business does not need.

The present international law on climate change, the UN Framework Convention on Climate Change and the Kyoto Protocol, are based on the principle of “common but differentiated responsibilities”. In other words different countries will undertake different commitments. This commitment will be carried forward to any new agreement which will, therefore, maintain the risk of “carbon leakage”. For example, if the EU commits to a higher level of CO<sub>2</sub> reduction than Ukraine, there is a risk that energy intensive production might move to this bordering country of the EU.

The degree of carbon leakage will depend on the extent to which other countries make comparable efforts in the various industrial sectors. For example, China could decide to base its emission reduction on a per capita basis or to concentrate its efforts entirely on the transport sector but not on the chemical or the steel sector. If different countries have different responsibilities on how to address climate change, the EU cannot and should not unilaterally determine the burden which those countries have to carry when exporting to the EU.

In the following I would like to make some specific comments:

- **Border measures could provoke a trade war**

If the European Union were to impose border measures against “climate sinners” it would probably start a trade war with huge and damaging consequences for European business. The target countries for the measures would most likely be the EU’s biggest trading partners, i.e. the United States and/or China. However, a trade war between the EU and either China or the United States is simply unrealistic since the EU, as the biggest exporting entity of the world, cannot have an interest in such a scenario. And BUSINESSEUROPE is not in the business of shooting its exporting companies in the foot on an issue like this.

I just want to underline this fact by some figures: the BUSINESSEUROPE Economic Outlook presented this Monday has shown that at present, exports are the main contributing factor supporting growth in Europe. This reflects to a large part the revival of global trade, following its collapse in 2009. Exports are expected to grow by more than 5% in 2010 and 2011, supported by a continued upswing in global demand.

- **Border measures will provoke retaliation and continuing WTO litigation**

The European Union has adopted several legislative acts to combat climate change, i.e. the European Emissions Trading Scheme (ETS). This instrument is based on caps of CO<sub>2</sub> emissions for installations – but does not relate to products as such. In other words, the ETS applies to chemical plants but not to the chemical products that are subsequently sold on the market. It is a fundamental difference if measures are related to products or production facilities. To introduce border measures, the EU would have to translate the domestic requirements into a justifiable measure on products with all the administrative difficulties this could entail. The background paper to this panel also clearly describes the difficulties that are linked to this.



The target countries will seek clarification in the WTO on whether such measures are WTO-compatible. Whatever form possible border measures would take, they are bound to become the subject of a long legal dispute in the WTO, entailing years of uncertainty for business. Indeed, border taxes on imports to compensate for the charges on EU producers would invariably lead to discriminatory taxation on imports – either between importing countries (“clean” exporters would pay the same tax as “dirty” exporters) or between exporters and domestic EU producers (EU plants that are benchmark producers pay less into the ETS than the average).

Other countries could also adopt border measures in the context of their climate change legislation, based on different considerations than the EU. Suppose an emerging country with low per capita CO<sub>2</sub> emissions bases its climate policies on a containment of per capita emissions and adopts border measures on this basis. Under such a system all exports both from the United States and the European Union would probably be subject to such measures since the per capita CO<sub>2</sub> emissions in the EU and the U.S. are much higher than in the emerging country concerned.

- **Applying border measures is a hugely bureaucratic exercise**

In many cases the products which are subject to cap and trade schemes in the EU are traded only to a limited extent or not at all. However, the derivatives of these products are widely traded. Whilst steel or cement may still be relatively easy to calculate the carbon content (but only for bulk products – not for sophisticated ones), for chemicals this would be an impossible exercise since it would require knowledge of the carbon content of thousands of derivatives.

- **Border measures will not reduce emissions but increase domestic budgets**

Border measures would have no environmental impact in the exporting country; the products would continue to be produced in that country and would, if not exported to the country taking the trade measure, be sold on the world market. Border measures would however have a positive impact on the budget of the importing country, however, in the case of export oriented countries the economic effects were only positive for as long as no retaliatory measures were taken by other countries. Supporting our state budgets would not appear to be a legitimate trade or environmental objective to me.

- **Border Measures will lead to trade diversion**

Some in Europe are suggesting a more sophisticated border measure scheme that would only apply taxes to imports from “dirty” or carbon intensive production sites. They are even calling for low carbon producers to potentially benefit from certificates to be sold on the EU carbon market. This approach would certainly be sophisticated but it would also contribute significantly to de-industrialisation in Europe.

If border measures were introduced the exports of products from “dirty” installation to Europe would probably stop. The exports into Europe from new third country installations would probably increase. Given the fact that new installations produce with the latest technology in a CO<sub>2</sub> friendly way they could be even from a CO<sub>2</sub> point of view be more competitive than the mature installations of the EU. It would be interesting for these installations to export to Europe notwithstanding the border



measures because they could compete. The “dirty” installations would not produce for the European market but for the world market. The EU products would not be able to compete with these products at the world market.

As the least developed countries would be exempted from the scope of border measures, it might, on the other hand, be interesting to invest in new facilities in least developed countries in order not to be subjected to these measures. This might be an interesting opportunity for developing countries, but it certainly is not the objective of the EU when introducing such measures.

I would like to come to a conclusion. As I have laid out in my presentation, unilateral domestic climate actions coupled with border measures will be ineffective with regard to global climate, yet could trigger a dangerous trade war. Therefore such measures should be rejected. Climate change is a global problem which should be addressed with coordinated, balanced and effective emission reduction policies at a global level.

Thank you for your attention, and I look forward to our discussion.

\*\*\*\*\*