

POLICY ISSUES FOR DEDICATED MULTILATERAL DISCUSSIONS ON BORDER CARBON ADJUSTMENT

COMMUNICATION FROM CHINA

The following communication, dated 10 November 2023, is being circulated at the request of the delegation of China.

In exploring trade policy responses to climate change, one type of policy focuses on carbon emissions associated with traded goods, making use of metrics of environmental policy instruments, such as carbon emissions, carbon intensity or carbon footprint. It seeks to apply trade policy tools, such as tariffs or border adjustments, to account for such emissions. Some measures of such hybrid nature are being rolled out in a unilateral manner, despite a lack of sufficient evidence, discussion or consensus on certain fundamental issues. These measures have triggered considerable controversy and have been subject to trade concerns and discussions in the WTO Council for Trade in Goods, Committee on Market Access, Committee on Technical Barriers to Trade and Committee on Trade and Environment, from different perspectives.

Building on China's two previous proposals¹, this communication focuses on one specific policy instrument, i.e. the border carbon adjustment (BCA), and proposes the following topics for dedicated multilateral discussions, to be held under the respective committees, as mandated, or under the multilateral deliberative mechanism on environmental sustainability, as proposed by several members.

The proposed discussions are intended to strengthen the linkages between the multilateral trading system and sustainable development, so as to seek *"both to protect and preserve the environment and to enhance the means of doing so in a manner consistent with their (Members') respective needs and concerns at different levels of economic development"*², and ensure that *"there should not be, nor need be, any policy contradiction between upholding and safeguarding an open, non-discriminatory and equitable multilateral trading system on the one hand, and acting for the protection of the environment, and the promotion of sustainable development on the other"*.³

1 THE BASIC OPERATING MECHANISM

1.1. **Carbon Leakage** – What is carbon leakage in the context of environmental policy? If there is gap in explicit carbon price between members, does it necessarily mean that there is a gap in the

¹ WT/CTE/W/251, A PROPOSAL FOR DEDICATED MULTILATERAL DISCUSSIONS ON THE TRADE ASPECTS AND IMPLICATIONS OF CERTAIN ENVIRONMENTAL MEASURES. Communication from China; JOB/TE/81, FURTHER ELABORATION ON DEDICATED MULTILATERAL DISCUSSIONS ON THE TRADE ASPECTS AND IMPLICATIONS OF CERTAIN ENVIRONMENTAL MEASURES. ENVIRONMENTAL MEASURES, Communication from China.

² Para. 1 of the preamble to the Marrakesh Agreement Establishing the World Trade Organization.

³ Para 4. of the preamble to the 1994 Marrakesh Ministerial Decision on Trade and Environment.

overall stringency of their respective carbon emission control policies? Can carbon leakage be used as a basis to justify the BCA?⁴

1.2. **Attribution** – How to objectively estimate the changes in the total amount and regional composition of global carbon emissions caused by the relocation of industries or import substitution? How to distinguish them from the changes in global carbon emissions caused by structural factors such as changes in the stage of economic development, the transition of the energy structure and the differences in factor endowments?

1.3. **Extra-territorial implementation** – When a Member imposes BCA on imports, is it regulating domestic carbon emissions or extra-territorial carbon emissions?

2 POLICY DESIGN

2.1. **Applicable Scenarios for BCA** – Which types of domestic policy measures related to carbon emission controls are suitable to be adjusted at the border? Which types are better suited to international coordination through multilateral approaches rather than a unilateral BCA? Are emission control measures on production facilities suitable for border adjustment?

2.2. **WTO Conformity of BCA** – When implementing BCA, how to ensure that the basic WTO principles of MFN treatment and national treatment? Where there are differences in the policy designs between domestic carbon emission control measures and their corresponding BCA, how to ensure that the policy burden imposed by the BCA on imported products does not exceed that imposed by domestic measures on the like domestic products, so as to avoid distorting market competition?

2.3. **Default values** – Default values for carbon emissions of imported goods seem to be a critical element in the policy design of BCA. Regarding setting the default values for extra-territorial carbon emissions, how to ensure the reliability of and minimize the time-lag in the database through effective cooperation with the members having appropriate jurisdiction, so as not to constitute arbitrary or disguised trade restrictions? What would be the basis to use the average emission intensity of the X% worst performing domestic enterprises plus certain markup as benchmark default values for emissions associated with imported goods?

2.4. **Carbon price under BCA** – Is it reasonable to benchmark BCA against the carbon price in emission trading market, when such carbon market has the attribute of a financial market and the resulted carbon price embeds a financial premium?

3 TRADE IMPACTS

3.1. **Unilateral BCA** – In what ways and what areas will unilateral BCA impact other members' international trade and macro-economy? How can the impacts of BCA on members' trade be measured in an objective manner?

3.2. **Carbon Club** – If a so-called Carbon Club, one that agrees to impose punitive tariffs on non-club members on grounds of differences in carbon intensity or carbon price, were formed to coordinate the implementation of BCA, what would be the impact on international trade?

4 ENVIRONMENTAL EFFECTS

4.1. **Nationally Determined Contributions (NDCs)** – What role will BCA play in a Member's achievement of its NDC under the Paris Agreement? In terms of extra-territorial carbon emissions, would targeted financial and technical assistance be better suited for reducing carbon intensity of imported goods?

4.2. **Use of revenues from BCA** – How should the revenues from BCA be used to better achieve the environmental goal of global carbon emissions reduction? For example, should it be used to

⁴ A thought provoking paper on this subject is NORDSTRÖM, Håkan, "Does the risk of carbon leakage justify the CBAM?" (2023/ 08), <https://cadmus.eui.eu/handle/1814/75367>.

compensate developing members whose trade are affected by BCA, in order to enhance their capacity to reduce carbon emissions?

5 INCLUSIVENESS

5.1. **Effective policy dialogues** – In designing and implementing BCA, how to make better use of multilateral platforms, such as the WTO, to promote effective policy dialogues with other members, on top of enhanced transparency? How should important factors identified in the course of the policy dialogues be taken into account in policy adjustments?

5.2. **Diversity and flexibility** – When designing and implementing BCA, how should a Member fully acknowledge and take in account the diverse range of mitigation efforts of other members, including but not limited to carbon pricing, effective carbon taxes, and other mechanisms that impose a price on carbon emissions?

5.3. **Data reporting and mutual recognition** – As members have notable differences in the energy and industry structure, production processes, carbon accounting methods, reporting cycles and so on, how can the differences in data reporting be accommodated in an inclusive manner when implementing BCA, so as to avoid additional and unnecessary costs to international trade? How can the mutual recognition of carbon emission data be realized in a scientific and reasonable manner?

5.4. **The Principle of Common but Differential Responsibilities (CBDR)** – How can it be reflected in the design and implementation of BCA?

5.5. **Disproportionate impacts by BCA on developing countries and SMEs** – How can the undesirable and disproportionate impacts of BCA be avoided for developing members that lack the infrastructure of carbon accounting, as well as for SMEs that have challenges in bearing the costs associated with data submission and third party verification?

6 OTHER ARRANGEMENTS

6.1. **Protection of submitted data** – BCA requires enterprises to submit carbon emissions and facility-specific data, some of which might be business sensitive or business confidential. If not duly protected, there is high risk of leaks, misuse or other type of data security issue. How to set the reasonable boundary for the data required? How to ensure the security of submitted data through institutional guardrails?

6.2. China welcomes contribution from other members with respect to additional policy issues regarding BCA as well as answers and solutions to these policy issues. We welcome written submissions by members and propose that the Secretariat circulate a compilation of members' written submissions with a view to informing further multilateral discussions. We believe that multilateral, structured and engaged discussions on such policy issues would be conducive to collectively strengthening the multilateral trading system and enhancing the complementarity of trade policy and environmental sustainability.
