AN INTERNATIONAL TRADE LAW PERSPECTIVE ON CLIMATE CHANGE

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ABSTRACT

International trade and climate change law are two distinct realms that inevitably and increasingly interact with each other. The relationship between climate change and international trade has been on a great verge of developing a new critical issue. With a quarter of global CO2 emissions directly or indirectly linked to the production and distribution of traded goods and services (World Bank, 2021), trade-related measures can play an important role in promoting climate change mitigation and adaptation. Policy and regime coherence are particularly important in the context of the international trading system. In a globalised world, trade influences emissions patterns worldwide. Trade rules also matter for the diffusion of climate-friendly technologies. Trade liberalization and environmental protection are held forth as irreconcilable objectives by some, whereas others suggest they are complementary. The main aim of this paper is to clarify and make transparent the requirements of international trade law pertaining to climate change policies and thereby allow negotiators to assess the credibility of a "WTO threat"-strategy. In this context the paper is divided into four sections. Section I provides the introductory part to all the multilateral and various other treaties ratified by the UN members for free trade and to counter environmental adversities raised. In section II Border carbon adjustments (BCA); a trade-related policy instrument to offset differences in the stringency of climate policies between trade partners is elaborated. WTO's new policy regulations regarding fossil fuel subsidies is discussed as part of section III. The article ends with analysis and concluding remarks.

Keywords: trade, climate, environment, treaty, carbon emission, fossil fuel.

I. INTRODUCTION

International economic law has an important role to play in the regulation of climate change, with respect to technology diffusion and unilateral responses to multilateral negotiation failure. In the case of the international trade law, deadlock at the multilateral level has led to unilateral, bilateral, and regional policy responses. The same may happen with respect to climate change negotiations. Climate change agreements should either comply with or prompt modifications international economic law and global models of economic governance. Existing international economic law places limitations on the right of national and sub-national governments to regulate to address climate change. Given the current difficulty in reaching multilateral agreements, for the most part countries will have to develop climate change policy and law within the constraints of the existing legal, economic, and financial framework. A further effect of international trade is its potential to improve the way we allocate resources.

Climate change law instruments − in particular, the UNFCCC and the Paris Agreement − constitute the legal framework within which States set emissions reduction targets and adopt climate mitigation measures to achieve the global target of limiting the increase in global average temperatures to "well below" 2°C. This legal framework leaves countries free to decide which measures they employ to achieve their targets. However, international trade law − and the rules and principles of the WTO − determines when and how States can adopt a measure which potentially impacts international trade, even if such a measure is primarily aimed at tackling climate change. Climate change related trade measures have a significant potential of reducing GHG emissions and are increasingly being adopted.

The UNFCCC requires industrialized countries and economies in transition to "adopt national policies and take corresponding measures on the mitigation of climate change, by limiting their anthropogenic emissions of greenhouse gases and protecting and enhancing their greenhouse gas sinks and reservoirs." Although national emission reduction targets were established in the Kyoto Protocol itself, it was left up to each individual country to choose which specific measures to adopt to meet their Kyoto Protocol target. UNFCCC and Kyoto Protocol are built upon the principle of "common but differentiated responsibility" with regards to the allocation of GHG emission reduction obligations between developed and developing countries. "The Parties should protect the climate system for the benefit of present and future generations of humankind, on the basis of equity and in accordance with their common but differentiated responsibilities and respective capabilities". The adoption of action plans on clean energy and climate-friendly technologies, which incorporate trade-related measures, has become quite common in nationally determined contributions. The United Nations 2030 Agenda for Sustainable Development identifies trade measures as an important tool to support the achievement of many of the 17 Sustainable Development Goals (SDGs) and foster transitions to a greener and more resilient economy. The Intergovernmental Panel on Climate Change (IPCC) has similarly stated that policies and instruments that can create incentives for mitigation actions include "regulations and standards, taxes and charges, tradable permits, financial incentives…" (IPCC, 2007) Trade related measures can contribute to States' efforts to "accelerate the development, deployment and dissemination of technologies, and the adoption of policies, to transition towards low-emission energy systems, including by rapidly scaling up the deployment of clean power generation and energy efficiency measures…" as indicated in the 2021 Glasgow Climate Pact.

The multilateral trade law under WTO auspices recognizes sustainable development and the protection of the environment as an overarching objective, thus paving the way for the adoption of WTO compliant trade measures addressing climate change. Trade related measures can be divided into tariff and non-tariff measures (NTMs). NTMs include a broad array of trade control instruments such as licenses, quotas, price control measures and finance measures as well as technical regulations. As technical NTMs can regulate product characteristics, production processes and import conditions, they are often adopted for environmental protection purposes (UNCTAD, 2022).

The widespread use and environmental effectiveness of NTMs has also been underlined by the IPCC, which pointed out the contribution of technical regulations to mitigation efforts in areas such as energy efficiency, consumer information (labelling), fuel standards and low emission industrial materials (IPCC, 2014 and 2022). Technical regulations generally set requirements that producers and retailers have to comply with in order to sell certain products on a given market. As such, they can be used to support the adoption of energy efficient technologies and the consumption of low carbon products by domestic consumers.

International standards are often used as a basis for technical regulations adopted at the national level, and WTO law urges Member States to base their technical regulations on international standards. In a recent analysis, the WTO highlighted the importance of international standards agreed by consensus in facilitating the transition to low carbon economies and in avoiding obstacles to trade (WTO, 2022b). For the purposes of the TBT Agreement, international standards are those prepared by the 'international standardization community'. The TBT Agreement makes reference only to the International Organization for Standardization (ISO) but the relevant case law has indicated other international standard setting bodies are able to develop 'international standards.' The TBT Agreement provides the necessary criteria for accepted International Standard setting bodies. Examples of international standards that are relevant for national climate change related technical regulations include standards to measure energy efficiency, such as those developed by the ISO to calculate the thermal properties of construction materials, or those developed by the International Electrotechnical Commission (IEC) to measure the efficiency of power conditioners. International standards can also provide guidance on how to quantify and report carbon emissions. Examples include standards ISO 14067:2018 for the quantification of the carbon footprint of products, or ISO 14064-1:2018 for GHG emissions and removal at the organizational level. Sectoral standards such as those developed by ISO on solar energy, hydrogen and wind technologies, and solid and liquid biofuels (WTO/UNEP, 2009) are another category of international standards of relevance for the adoption of technical regulations.

Recent years have seen a surge in WTO disputes targeting domestic support and policy measures related to clean energy, leading to potential contradictions between the trade regime and climate action. The case-by-case nature of WTO disputes does not provide sufficient structural legal guidance for the implementation of NDCs under the Paris Agreement, and leaves the settlement of climate related disputes to a body that is guided first and foremost by the rules of the multilateral trading system. As multilateral initiatives and decisions to create room for climate change policies and measures have their own difficulties and challenges, particularly owing to the large number of WTO Members (164 at present), advancing climate change objectives among a smaller group of like-minded countries is an avenue worth exploring – either through plurilateral initiatives or through regional trade agreements (RTAs). RTAs also offer opportunities for policy experimentation through which states can craft and test climate provisions at a limited scale with like-minded countries. Besides, RTAs are uniquely positioned to address various measures at the intersection of trade and climate change, such as the transfer of low-carbon technologies, emissions trading, BCAs and fossil fuel subsidies, to name a few. RTAs can further help in setting common rules for trade-related climate measures by aligning standards and regulations. Finally, climate measures agreed at the regional level may potentially be multi lateralised at a later stage. Hufbauer and colleagues have proposed a plurilateral trade and climate code which would deal with a range of aspects at the intersection of climate and trade. The International Centre for Trade and Sustainable Development has suggested a 'Sustainable Energy Trade Agreement' covering the liberalisation of trade in climate-friendly goods and services.

II. BORDER CARBON ADJUSTMENTS AND STRATEGIC CLIMATE POLICY

Border carbon adjustments are trade-related policy instruments to offset differences in the stringency of climate policies between trade partners. They do so by imposing a tax or other regulatory measure on imports based on their carbon content and/ or by exempting exports from domestic carbon constraints. BCAs have been periodically discussed as a way to address concerns about emissions leakage (when climate action in one region merely shifts the incidence of emissions elsewhere) and to incentivise climate-laggard nations to adopt more ambitious climate policies. Because they differentiate goods based on their carbon footprint, however, BCAs affect trade and are seen as being at risk of violating WTO rules. Some consider them a form of green protectionism.

Proponents suggest that such measures would reduce carbon emissions, protect domestic firms from unfair competition, and provide incentives for carbon intensive exporters to clean up their act and sign a multilateral climate agreement. A BCA can provide the exporter with incentives to adopt a more stringent climate policy, incentives that a tariff does not provide. The BCA's effect on the exporter's incentives has two components. The first is the change in the exporter's terms-of-trade. This alone induces the exporter to adopt a weaker climate policy and is the only component when the border measure is a tariff. The second component captures potential climate policy benefits, which arise because of the fundamental difference between the tariff and the BCA: the BCA drives a wedge between consumer prices at home and abroad that is a function of the emission taxes, i.e., the magnitude of the BCA is decreasing in the exporter's emission tax. However, these climate policy benefits can induce the exporter to adopt a stronger climate policy only if the exporter's climate policy is weak. This suggests that a necessary condition for the BCA to induce the exporter to adopt a more stringent climate policy is that the exporter cares about climate damages. It might be better to deploy a BCA/tariff to leverage the exporter's climate- policy and target global emissions. This would emphasize a BCA design that recognizes the exporter's climate policy efforts. Without this feature, the BCA may be no different from a tariff in terms of effects on the incentives facing the exporter's climate regulators.

III. FOSSIL FUEL SUBSIDIES

The adverse environmental, economic and social implications of the sizable subsidies handed out by governments for the production and consumption of fossil fuels are increasingly clear. The sheer size of these subsidies is a significant burden to the public purse. Although estimates by different international organisations vary, even the most conservative amounts are huge. For instance, a relative conservative estimate by the Organisation for Economic Co-operation suggests that fossil fuel subsidies added up to US$ 373 billion in 2015. These fossil fuel subsidies also divert investment from other, often more pressing, development objectives such as health care and education. Moreover, by promoting the burning of fossil fuels, they contribute to climate change and help lock in carbon-intensive energy systems. Importantly, by affecting fossil fuel prices, subsidies can have distorting impacts on trade and investment. As WTO Members are slowly making progress in the negotiations to create new disciplines for another type of environmentally harmful subsidies, those for fisheries, a range of options has been put forward to address through the WTO fossil fuel subsidies too. However, the implementation of any of these options will likely face the same political and legal hurdles that made WTO action on this issue challenging thus far. These include the fact that WTO law at present 'under-captures' fossil fuel subsidies compared to renewable energy subsidies. This is because fossil fuel subsidies are often not 'specific' in the sense of the WTO Agreement on Subsidies and Countervailing Measures, and adverse trade effects caused by them are difficult to prove. Perhaps therefore fossil fuel subsidies have not been challenged before the WTO dispute settlement system. Finally, with regard to fossil fuel subsidies, it is notable that some options are already being pursued by WTO Members, namely improving transparency by flagging fossil fuel subsidy reform in the WTO's Trade Policy Reviews, and adopting political declarations. These options can be regarded as initial steps to address fossil fuel subsidies through the WTO. Such steps can be taken by small groups of WTO Members working together (including, but not necessarily limited to, the Friends of Fossil Fuel Subsidy Reform), and do not require action by the entire WTO membership. Further options in this regard in the short to medium term include new actions by small groups of WTO Members, such as adopting a pledge-and-review model, and slowly building critical mass for addressing fossil fuel subsidies through international trade agreements, such as through future political declarations.

Given the hurdles of a legal reform of the WTO regime, the policy options that focus on ushering in procedural changes in trade- as well as climate related institutions and practices appear to be politically more promising in general. For instance, including climate-related technical expertise in the WTO dispute settlement may not only help clarifying the technicalities of the climate measures under scrutiny, but also expedite the dispute resolution process. Given that a legal window for including climate-related technical expertise in dispute panels already exists, the implementation of this option may not face insurmountable political barriers in the near term, notwithstanding the ongoing impasse at the Appellate Body over the stalled appointment of judges. Procedural reform could also mean making more effective use of the existing forums under the WTO and UNFCCC. Doing so could help to apply and interpret laws and promote integration of climate concerns in trade matters, which eventually improves legal certainty. As for the WTO Trade Policy Review Mechanism, while the mandatory inclusion of climate-related impact assessments may not be feasible any time soon, particularly in the absence of a legal basis under WTO law, voluntary disclosures could be achievable in the near term.

IV. ANALYSIS AND CONCLUSION

Advancing climate change objectives among a smaller set of like-minded countries is an avenue worth exploring further, either through plurilateral or regional trade agreements. Although plurilateral talks on the Environmental Goods Agreement made some initial strides, negotiations have stalled since December 2016. The EGA still stands a reasonably high chance to advance the climate agenda by facilitating the diffusion of climate-friendly goods and technologies, but much depends on how far the fundamental difficulties to establish definitions are overcome as and when negotiations resume. As for regional trade agreements, the EU has played a pioneering role in leveraging this route, more recently going as far as refusing to sign trade deals with countries that have not ratified the Paris Agreement. While other countries could potentially follow the EU's lead, the political feasibility of including climate-related provisions in new or existing RTAs will likely vary from one country/region to another. While including binding climate-related provisions in prospective RTAs is likely to be challenging, the prospects would increase if the provisions were voluntary in nature. In the short term, the review and renegotiation of existing RTAs for climate purposes is likely to be more difficult to accomplish politically Many of the considerations that apply to general changes to the multilateral trade regime also extend to the specific area of border carbon adjustments. If anything, their controversial nature would make taking any step requiring consensus or approval by all or a vast majority of WTO Members even more challenging. Also, a substantial body of academic literature suggests that, depending on their underlying intent and nuances of their design and implementation, BCAs could very well be legally viable already under current WTO law. While additional steps, such as an amendment of WTO rules, a waiver or an authoritative interpretation may increase legal certainty in the short term, these could also convey that BCAs are illegal in the absence of such changes, and narrow down the flexibility afforded to WTO Members under the existing legal framework. Overall, the current gridlock in multilateral trade negotiations suggests that any meaningful progress on BCAs as a tool of climate policy will most likely take shape at a regional level, with a coalition of like-minded countries advancing the concept on a reciprocal basis. Such cooperation may, over time, become a catalyst for broader and eventually multilateral action. But again, the short-term prospects for coordination on BCAs under the multilateral trade regime are dim.

At last, international co-operation on climate change policies will best be achieved in an international climate of trust. Improved policy integration across different governmental departments on the climate change issue is a pre-condition for this and will lay the ground for developing further international cooperative agreements on the co-ordination of climate policy measures or on the mutual recognition of, for instance, energy efficiency standards developed in other countries. Presently though, trade and economic ministries of industrialised countries are busy questioning the WTO-compatibility of other countries' climate change programmes long before details about specific measures have come to the fore. The obstructive effect of such influences on domestic legislative processes is well documented by a range of case studies on environment and international competitiveness.

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