

CO₂ Border Adjustment as a Source of Revenue for the EU Budget?

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The draft law on the European Carbon Border Adjustment Mechanism (CBAM) is currently being discussed in the European Parliament's Committee on Environment. A vote is scheduled for the end of February. If it comes to a vote, a majority in the committee, and subsequently in the European Parliament and the European Council, is considered relatively certain.

However, the proposed CBAM is problematic regarding WTO conformity (World Trade Organization), because it violates two of the organisation's basic principles: Since the level of the levy depends on the CO₂ emissions caused during production and consequently does not treat all importers equally by its very nature, it violates the principle of most-favoured-nation treatment. According to this principle, all importers are entitled to treatment in line with the most favoured WTO member. In addition, the law would maintain the free allocation of allowances in the European Emissions Trading Scheme (EU-ETS), at least for a transitional period. Since the CBAM already compensates for price advantages of foreign importers, this would give European companies a double advantage and would thus violate the principle of national treatment, according to which importers may not receive less privileged treatment than domestic producers.

A way to circumvent these issues could be a reference to Article 20, Paragraph g, GATT, which allows exceptions for the conservation of exhaustible natural resources. Accordingly, however, it would then have to be clear that the CBAM is exclusively used as an instrument of climate protection – and does not also serve to protect European industry and generate new revenues. It would therefore be important for revenues from the CBAM to be earmarked for climate protection measures. This is not provided for in the present draft; on the contrary, the draft insistently advertises the fact that the revenues should contribute to the general EU budget as a new source of own EU-resources. Ideally, how-

ever, the revenues from the CBAM would flow into developing and emerging countries to help them restructure their CO₂-intensive industries affected by CBAM. This would come at no additional cost to the EU, given that such measures are planned anyway and are a vital component of the EU's propagated role as a global pioneer in climate protection and for its contribution to global emissions reduction.

With CBAM revenues flowing directly into this pot, fewer financial means would have to be taken from the EU's general budget. Such a solution would not only bring the CBAM closer to WTO compliance in formal terms but would also increase the chances of it being realistically implemented. After all, the introduction of a trade instrument can only be prohibited by the WTO if challenged by another WTO member. If this does not happen, it can remain in force even if it is not WTO-compliant in principle. With the proposed solution, emerging countries affected by the CBAM would no longer have an incentive to file a complaint against the CBAM.

Transferring the CBAM revenues to the general budget and thus increasing the likelihood of a challenge before the WTO also does not seem well thought out given that the expected revenues are not particularly high. Dröge (2021)¹ has simulated this for the eight most important trading partners in each of the sectors of cement, energy and pig iron, steel, and ferroalloys. Depending on assumptions regarding the further free allocation of ETS allowances, she arrives at sums totaling between 397 million and 3.2 billion Euro annually.

Although this does not cover all importers and sectors, it shows that realistically one should not expect more than a low single-digit billion amount annually, and this sum should steadily decrease as trading partners can be expected to fall under the CBAM less frequently through increased climate measures on their part. In terms of the EU budget, this represents an insignificant amount.

We therefore propose to amend the bill so that the revenues generated through the CBAM are to be earmarked for climate action.

More information on the topic: <https://www.kas.de/documents/252038/11055681/Just+enough+-+the+EU+proposal+for+a+carbon+border+adjustment+mechanism.pdf/f4568873-4e16-d885-593b-0966c16af50b?version=1.0&t=1625065236601>

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- 1 Susanne Dröge (2021): Ein CO₂-Grenzausgleich für den Green Deal der EU – Funktionen, Fakten und Fallstricke. SWP Studie 9, July 2021, Berlin.

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