

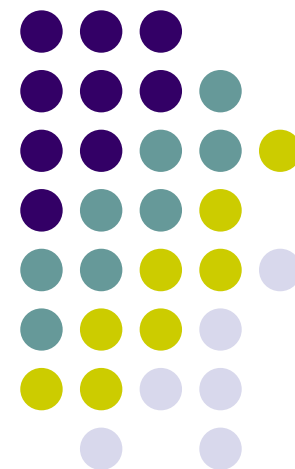
# Reconciling Climate Policy with the International Trading System

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# US Climate Change Policy



- **President Obama and Congressional leaders will take domestic action on climate change**
  - Impose cap-and-trade system (economy-wide).
  - Develop low carbon technologies, possibly with large subsidies.
  - Stimulus package includes energy provisions (energy efficiency projects, electricity grid, guaranteed loans for renewable energy, renewable energy research).
  - May use EPA CO<sub>2</sub> limits as a hammer both for legislation and international action.
  - However, in the wake of the financial crisis and recession, climate change legislation will probably not be enacted before 2010.
- **Obama also promises active role in Copenhagen**
  - President will want progress on domestic climate legislation to strengthen his hand in reaching an international agreement.
  - But he will not want US position carved in stone before the international accord.

# UNFCCC and the WTO



- **Copenhagen Regime**

- The Kyoto protocol expires in December 2012 and its successor regime is meant to be agreed in Copenhagen in December 2009.
- In Copenhagen, countries may reach agreement on emission targets and time paths with pledges by both developed and developing countries (common but differentiated responsibilities).
- But each country chooses own methods to meet targets.

- **The WTO**

- In recent speeches, Director-General Pascal Lamy has suggested that norms agreed to in Multilateral Environment Agreements (MEAs) would be taken seriously at the WTO.
- Linking climate change to future WTO negotiations
  - ❖ Define “environmental goods” and revise tariff schedule.
  - ❖ Initiate sectoral agreements on climate that would restrict international trade in designated goods to countries with qualifying greenhouse gases (GHG) emission limits.

# Competitiveness Issues

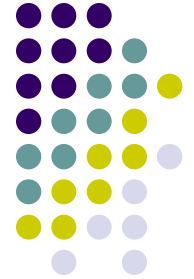


- **“Leakage” and “Leverage”**
  - Domestic action alone might weaken US firms and lead to the “leakage” of production and jobs to foreign firms.
  - Congress also wants to create “leverage” to encourage developing countries to limit their own rapidly growing emissions.
- **To address these concerns, many US climate bills include specific provisions**
  - Free allocation of allowances, special exemptions, border adjustments
- **Border measures are certain**
  - Many US climate bills include border measures that impose limits on imports from countries that do not have comparable climate policies.
  - Export rebates seem likely.
  - Issues: potential for retaliation / questionable leverage / WTO legality

# Justification under the WTO



- **Both import restrictive measures and measures that appear to subsidize exports stand a fair chance of being challenged in the WTO**
  - Unilateral systems of import bans, border taxes, and comparability mechanisms could cause a drawn-out period of trade friction.
  - Existing WTO jurisprudence leaves ample room for conflicting interpretation.
- **Relevant WTO provisions**
  - GATT Articles I (MFN), II (tariff schedule), III (national treatment), XI (quantitative restrictions), and XX (general exceptions)
  - The Agreement on Subsidies and Countervailing Measures (ASCM)



## Article XX (general exceptions)

- **Article XX (general exceptions) may provide a “safe harbor” for trade measures. However, the measures must conform to the demanding chapeau of the Article. The chapeau of GATT Article XX reads:**

*"Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures"*



# Table 1. Border Measures and GATT Articles

Restriction on imports of goods		Justified under General Agreement on Tariffs and Trade (GATT) articles?				
		Article I (Most favored nation)	Article II (Tariff schedules)	Article III (National treatment)	Article XI (Quotas)	Article XX (Exceptions)
Import restriction applied to penalize "foreign-emitted carbon" (measures applied only against imports)	Import ban (quantitative restriction)	Status unclear		(Covered under Article XI)	No, because violated.	<p>Yes. If any provision or restriction on imports can be justified under Article XX, it is permitted even though it violates other GATT rules.</p> <p>Recourse to an Article XX exception is scrutinized carefully and the burden of proof is on the country seeking to invoke the exception.</p> <p>The measure has to qualify under a specific exception in Article XX, such as Article XX(g) as a measure relating to the conservation of exhaustible natural resources. In addition, the measure must meet the test in the Article XX chapeau, namely, that the measure is not applied in a manner that constitutes arbitrary or unjustifiable discrimination or as a disguised restriction on international trade.</p>
	Additional or punitive tariff	No, because punitive tariffs will differ between foreign countries.	No, because it violates bound tariffs.			
	Antidumping or countervailing duties	No. Under present GATT rules, even if the exporting country does not restrict its carbon emissions, the social cost of carbon cannot be labeled as dumping or a subsidy. The failure to impose a carbon tax, or otherwise internalize the full price of carbon, does not currently give other World Trade Organization members the right to impose penalty duties on imports. Such measures would violate the Agreement on Subsidies and Countervailing Measures and the Antidumping Agreement for which no Article XX exception would be available.				
Competitive provision applied as an extension of domestic US climate policy (measures applied both to domestic production and imports)	Carbon tax on products	Yes, if the tax is imposed on the product and is not based on the country of origin.		Not violated. Carbon taxes on products can be justified as an "internal tax" under GATT Articles III:2 and II:2(a) and thus can be adjusted at the border.		
	Cap-and-trade system with applicability to imports	No, if foreign countries are treated differently.		A violation would occur if imported products are treated less favorably than like domestic products.		
	Carbon performance regulation applied to products and the production process	No, if foreign countries are treated differently.		A violation would occur if imported products are treated less favorably than domestic products. (The Agreement on Technical Barriers to Trade may also be implicated.)		

# Dispute Approach vs. Code Approach



- **Dispute Approach**
  - Let the WTO dispute settlement process run its course.
  - This approach foretells a long period of uncertainty and trade frictions and will put great pressure on the WTO system.
- **Negotiation Approaches**
  - Amendment or Waiver? – Not practical
    - ❖ Requires a consensus of members for amendment and at least three-fourths approval for a waiver.
  - A New Code of Good WTO Practice on GHG Emission Controls
    - ❖ A plutilateral agreement (say 10 countries) under Annex 4 of the WTO agreement, or a new code adopted outside of the WTO seems practical.
    - ❖ The Code would define the policy space for climate control measures that are consistent with core WTO principles.
    - ❖ A “peace clause” among key emitting countries would suspend border measures to allow WTO negotiations.