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Border Tax Adjustments

**Reducing Leakage from Unilateral
Implementation of Emissions Trading**





I. Border Tax Adjustments – The Rationale

- Climate change requires price signal on Carbon
- Different willingness in different countries
- Result may be **leakage**



II. Definition

Border Tax Adjustments (BTA) are fiscal measures designed to

- (i) **relieve *exported products*** of some or all of the tax charged in the exporting country in respect of similar domestic products sold to consumers on the home market; or
- (ii) **impose on *imported products*** some or all of the tax charged in the importing country on similar domestic products

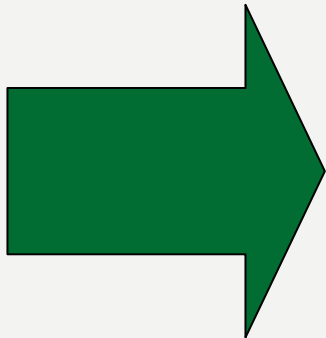


III. Importance of Legality under WTO

- Otherwise possible retribution
- Maintains good-will
- Provides confidence for investors (long-term sustainability of scheme)
- No clearance mechanism

III. Importance of Legality under WTO

- Illegal subsidy/discrimination?
- Justification for discrimination?



Avoid illegal
subsidy/discrimination
AND/OR
Provide justification



1. Illegal Subsidy/Discrimination

a) EXPORTS: Avoid Illegal Subsidy!

- Prior-stage cumulative taxes adjustable
- Allowances as taxes?
- Adjustable taxes? Only if incorporated!
Fn. 61 to Annex II?
- At what level?



1. Illegal Subsidy/Discrimination

b) IMPORTS: Avoid discrimination under Art. III: 2 Sent. 1 GATT ("like products")

Product based

- Energy input incorporated?
- No discrimination if deemed usage of best available technology
- Alternative: use average, and allow for refuting conjecture?



1. Illegal Subsidy/Discrimination

- c) IMPORTS: Avoid Discrimination under Art. III: 2 Sent. 2 GATT (Directly competitive and substitutable products)



1. Illegal Subsidy/Discrimination

d) IMPORTS: Most Favored Nation Treatment
under GATT (Art. I GATT)

Participation in Kyoto as reason for different
treatment?



2. Justification under Art. XX GATT

Two tier structure:

- a) Any of the eight headings
- b) Chapeau

Judiciary has sometimes been generous;
yet example of ECJ suggests, where available,
avoiding discrimination is safer option



V. How to Implement It?

- Focus on *sector specifics* not *generalised solutions* to counter general protectionism
- Focus on *leakage, not competitiveness*
- Challenge to take it forward with international coalition, so as to support stringent climate policy, rather than undermine good will of countries



V. How to Implement It?

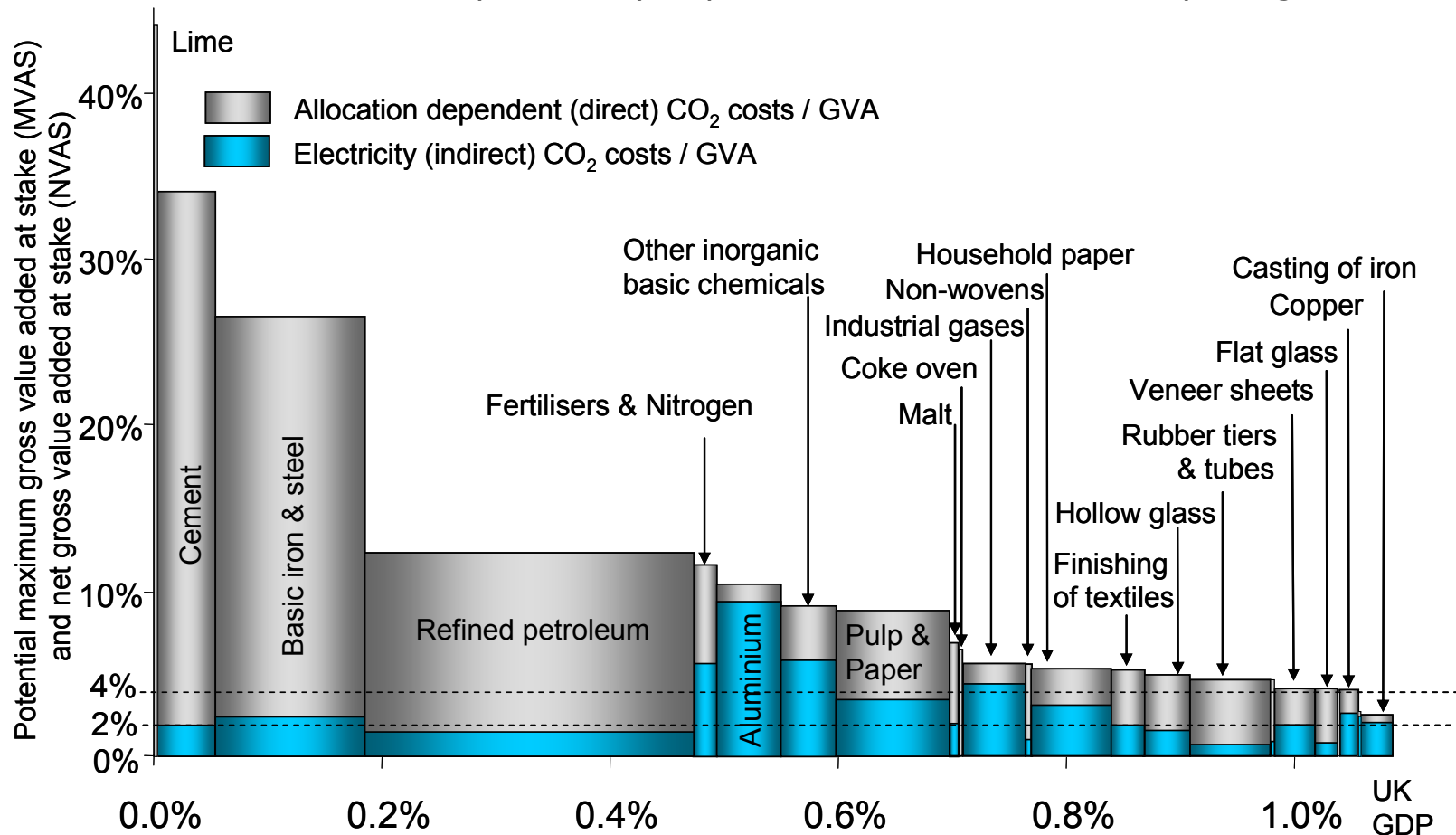
What are relevant sectors?

- Cement
- Certain steel
- Chemicals where evidenced

BTA for electricity presents challenges

Competitiveness impacts in a world of unequal action are not macroeconomic, but sectoral for a few specific cases

CO2 cost screen: Sectors potentially exposed under unilateral CO2 pricing



Price increase assumption: CO₂ = €20/t CO₂, Electricity = €10/MWh



VI. Conclusion

Border tax adjustments can

- Reduce leakage
- Be legally feasible
- Be targeted (and should!)

Alternative: Export taxes as proposed by Mueller (2005) with different incidence; imputation?