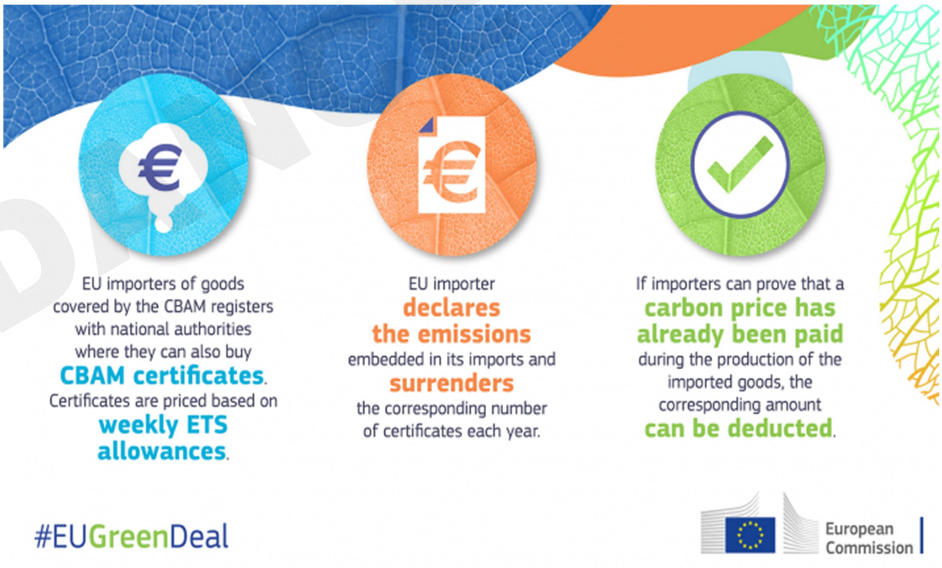
Climate Change: European Union's Carbon Border Adjustment Mechanism and its impact on India:

Syllabus: GS 3 Mains - *Conservation, Environmental Pollution and Degradation, Environmental Impact Assessment*.

2021 has already left its mark on global discussions about trade and the climate change. Recently, the EU proposed a levy on imported carbon-intensive products.

What is a carbon border adjustment tax? What is driving the EU in that direction?

- A carbon border adjustment tax is a **duty on imports based on the amount of carbon emissions** resulting from the production of the product in question.
  - As a price on carbon, **it discourages emissions**.
  - As a trade-related measure, **it affects production and exports**.
- Recently, the EU declared it would cut its carbon emissions by **at least 55%** by 2030 compared to 1990 levels. EU's greenhouse gas emissions have fallen by 24% compared to 1990 levels. But imports from emissions--**which contribute 20% of the EU's carbon dioxide emissions--are increasing,** the resolution said. Such a carbon tax would incentivize other countries to reduce GHG emissions and further shrink the EU's carbon footprint.



  - In proposing a Carbon Boarder Adjustment Mechanism (CBAM), the **EU claims to be concerned with the relocation of production to countries with less ambitious climate policies,** undermining EU's and global climate objectives. For the EU, CBAM would be neither a tax nor a tariff, but a policy measure.
  - Also, by '**equalizing**' the price of carbon between domestic products and imports, the **EU claims to promote fair competition, levelling the playing field** between EU and non-EU businesses.

How are other countries responding?

- If designed unilaterally, it **tends to be seen as unfair by** trading partners. There is the risk that it becomes a protectionist device, unduly shielding local industries from foreign competition in so-called ***'green protectionism'***.
- The EU's CBAM proposal contains various controversial aspects. For example: how to fairly account for emissions related to the production of imported goods? How to duly consider the costs that companies already face in complying with climate regulations in exporting countries?
- The United States, China, India, Brazil, South Africa and several others, including least-developed countries, have expressed concern over the EU's CBAM.
- The **BASIC** (Brazil, South Africa, India and China) countries' grouping had opposed the EU's proposal in a joint-statement, terming it "discriminatory" and against the **principles of equity** and **'common but differentiated responsibilities and respective capabilities' (CBDR-RC).**

> **CBDR-RC** principles acknowledge that **richer countries have a responsibility of providing financial and technological assistance to developing and vulnerable countries** to fight climate change.

- Assuming that the bloc will move ahead with the proposed scheme, what are the options for EU's trading partners?
- **Partners may:**
  - **choose to retaliate imports coming from the EU**: Countries could decide to impose barriers on EU imports in response.
  - **adopt their own CBAMs:** Following the EU announcement, the US is now considering this. A similar scheme is in the making in Canada.
  - **challenge the EU CBAM**: Trade specialists have been discussing the consistency of the EU proposed mechanism with multilateral rules. A WTO dispute against the EU is possible.
  - **choose to negotiate exemptions with the EU:** Some partners feel that they are being forced into negotiating with Brussels, as the proposed CBAM scheme allows for the EU to acknowledge the costs of climate policies on the production abroad. But negotiating exemptions with the EU ultimately means bowing to a scheme often seen as an imposition from Brussels on others.

How does this impact India?

- As India's third largest trading partner, the EU accounted for €62.8 billion ($74.5 billion) worth of trade in goods in 2020, or 11.1% of India's total global trade. India's exports to the EU were worth $41.36 billion in 2020-21, as per data from the commerce ministry.
- The EU's resolution stated that to begin with, by 2023, the **CBAM would cover energy-intensive sectors such as cement, steel, aluminum, oil refinery, paper, glass, chemicals as well as the power sector**.
- By increasing the prices of Indian-made goods in the EU, **this tax would make Indian goods less attractive** for buyers and could shrink demand.

How can all parties make the most of the EU's move?

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- A proliferation of different carbon border measures would create **unnecessary costs to trade**, in addition to **more room for discrimination and protectionism**. Importantly, in the absence of coordination, only suboptimal climate results would emerge.
- With the proposed CBAM, there is a new sense of urgency for a shared understanding on carbon-based trade policies. If countries believe a carbon border tax is the way forward, a global view on this topic should include an alignment of key parameters applicable to them, as well as agreed standards for measuring carbon that is emitted in the production of goods.
- **Transparency** and **non-discrimination** should remain key principles of any global understanding, and that should also ensure that carbon-related measures do not unnecessarily restrict trade. **A shared vision should also recognize, in line with the Paris Agreement**, that countries observe different approaches and speeds in their decarbonization efforts.

It is also noteworthy that, The EU proposal brings trade and climate decisively together. With civil society and businesses, leaders must seize this opportunity to promote coherence between climate and trade regimes, maximizing both environmental and economic benefits.