

# **EU CARBON BORDER TAXATION & ITS IMPLICATIONS TO THIRD COUNTRIES**

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## AudIT-S project

“Legal and financial significance of sustainability audit schemes through smart data management”

Spanish Ministry of Science & Innovation (PID2019-105959RB-I00)

<https://www.ucm.es/proyecto-audit-s/>



## Committee of Experts on International Cooperation in Tax Matters

### Committee of Experts on International Cooperation in Tax Matters Twenty-fourth session

4-7 April and 11-12 April 2022

Item 3(g) of the provisional agenda

#### Environmental Taxation

#### Co-ordinators' Report

##### *Summary*

At its 23rd Session, the Tax Committee decided to consider emerging issues in environmental taxation and address critical topics that were either not covered in the UN Handbook on Carbon Taxation (2021) or were covered there but not sufficiently and to this end established the Subcommittee on Environmental Taxation and its specific mandate.

The Subcommittee met for the first time on 28 January 2022 to consider the topics of immediate relevance for developing countries that could be included in its proposed 2022-2025 work plan.

The Subcommittee now presents this document to the Committee and seeks its **approval** of the proposed work plan (as set out in **paragraphs 6 to 9** of this CRP and described further in the **Annex**). The Subcommittee proposes to produce short papers on the critical aspects during the mandate, with the possibility of the short papers being compiled and published as one volume at the end of the mandate (as set out in **paragraph 12** of this CRP). The proposed areas are as follows:

- (a) *the interaction of carbon taxation with other national measures, including (but not limited to) in the context of broader tax reform and particular attention to fossil subsidies;*
- (b) *the role of carbon taxes and other measures to support energy transition;*
- (c) *the interaction between carbon taxes and carbon offsetting programs; and*
- (d) *Carbon Border Adjustment Mechanisms and how developing countries can avoid undesired spillover effects from other countries applying those measures.*

- ✓ Climate objectives: CBAM to fight carbon leakage
- ✓ Impact on developing countries: econ, envt'l & adm
- ✓ Alternatives & justification
- ✓ Reactions by UNCTAD, G7 & European Parliament
- ✓ Final remark

Carbon leakage: shift sourcing/move production to reduce costs of decarbonisation measures

Firms may lose sales to foreign competition

(less profits -> employment -> tax collection)

+ energy intensive trade exposed sectors

(iron & steel, aluminium, cement, fertilizer, glass)

EU Commission proposed CBAM to reduce this risk (ensure that the prices reflect accurately carbon content)

⇒ uncertainty on 3<sup>rd</sup> States governments' + corporations operating in developing countries

⇒ sensitivity re technical difficulties & administrative burden:

- exemption- electricity market
- agreements with 3<sup>rd</sup> countries to consider the carbon price paid in origin
- Phase-in period simplification (report, not pay)

Emissions increase in countries with lower carbon pricing  
Econ impacts on their tax base & industries (direct costs + indirectly)  
decrease national income, limit export potential

Ex. Low income countries, such as Tajikistan and Zimbabwe, and least developed countries, such as Mozambique, would be vulnerable

MNE will need to go through verifications process of complex supply chains  
(limiting eligible verifiers to those accredited to the EU might impose an undue cost on importers)

UN Subcommittee: How developing countries can avoid undesired spillover effects from CBAMs (Canada, EU, Taiwan, UK, US)?

The US bill grants exemptions to the countries that are on the most recent development assistance committee list of least developed countries and any country which has stringent environmental regulations to limit GHG emissions

## Alternatives to address leakage:

- issuance of free permits under an ETS
- reduced rates of carbon tax
- output based pricing systems

Article (2) (2) Paris Agreement: implementation to reflect equity, **principle of common but differentiated responsibilities &** respective capabilities, in the light of different national circumstances

Devise an inclusive scheme to help developing countries with financing and pricing

methodology for calculating embedded emissions, monitoring throughout the value chain, verification and certification tools impact reliability

## Developed countries can offer:

- technological capacity to reduce carbon emissions
- low-interest financing
- favorable bilateral trade programs (transparency & cooperation with close trading partners)

**UNCTAD (2021) CBAM** reduces the leakage **but** the real emission reductions come from the domestic carbon pricing

- Targeted exemptions would open the CBAM to criticism of ‘resource shuffling’ (when importers of electricity ensure low carbon imports, but the electricity produced locally has higher carbon footprint)

**G7 Summit Elmau, 28 June 2022 “Statement on Climate Club”**

Boosting international ambition through partnerships and cooperation. This includes promoting a just transition and providing support for developing countries

**EP** The Committee on Environment, Public Health and Food Safety adopted its report on the CBAM on 17th of May 2022

Transfer of CBAM revenues to least developed countries / financial support to these countries

On 22 June 2022, the Parliament adopted its position: phasing in with extended deadlines, broadening the scope & mentioned that **revenue from CBAM shall accrue to the EU budget, and be reflected in an increased support to least developed countries decarbonisation efforts**

(55) As the CBAM aims to encourage cleaner production processes, the EU stands ready to work with low and middle-income countries towards the de-carbonisation of their manufacturing industries. Moreover, the Union should support less developed countries with the necessary technical assistance in order to facilitate their adaptation to the new obligations established by this regulation. ***While the revenues generated by the sale of CBAM certificates will enter the Union budget as general income and should not be assigned to any specific Union budget expenditure, in light of the universality principle governing the Union budget, the Union should finance least developed countries' efforts towards the de-carbonisation of their manufacturing industries with an annual amount corresponding at least to the level of revenues generated by the sale of CBAM certificates. Such funding should be provided through the financial support provided by the Union to international climate finance and the relevant geographic programmes and the thematic programme Global Challenges of the Neighbourhood, Development and International Cooperation Instrument established by Regulation (EU) 2021/947 of the European Parliament and of the Council<sup>1a</sup>. The necessary adjustments to the budgetary appropriation of that instrument should be made through the Union annual budgetary procedure until 2027 and then included in the next multiannual financial framework.***

**Amendment** 130 Proposal for a regulation **Article 24 a (new)** Revenues generated by the sale of CBAM certificates

- ✓ A disproportionate burden on developing countries could make CBAM implementation fail
  - => Devise equitable and feasible mechanisms to support developing countries in their reduction of carbon emissions (Country specific incentive programs + technical assistance)
- ✓ Collaboratively establish alternative and/or supplementary measures
  - => Cooperative efforts are key to successful implementation
- ✓ Only with fairness the goal of environment protection will be attainable
  - => Provide technological, trade, administrative & financial support

# Thank you

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