Annex II

The EU CBAM Proposal, UNFCCC and the Paris Agreement

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I. Introduction

1. The EU Commission Proposal for a Regulation of the European Parliament and of the Council establishing a Carbon Border Adjustment Mechanism [COM(2021) 564 final, 14.7.2021] as amended by the Council and by Parliament in 2022[1], raises considerable anxieties among trading partners of the EU, in particular in developing countries.[2] The proposal introduces an obligation to importers in dedicated sectors and goods (Annex I of the proposed regulation) to buy on an annual basis CBAM certificates per ton of embedded emissions of such imported goods commensurate to the average price of EU internal market emission trading.

2. Additional costs on imports induced primarily intend to deter carbon leakage, i.e. the relocation of domestic production subject to carbon-emission trading requirements to countries operating lower production standards. They also intend to foster and encourage structural adjustments to sustainable modes of production abroad. The financial proceeds of the measure are destined for use in the general budget of the EU. They are not specifically earmarked to support transfer of technology to third countries with a view to accelerate the reduction of carbon emission abroad. The proposal, instead, refers to official development assistance (ODA) as a means to support developing countries:

> [T]he introduction of CBAM certificates based on actual emissions would protect against the risk of carbon leakage while incentivising third country producers to move towards cleaner production processes, with the support of Official Development Assistance when applicable" (p. 9/10).

3. Trading partners of the EU, in particular developing countries, are afraid that the measure removes comparative advantages and deploys protectionist effects and runs counter to the principle of shared but differentiated responsibility under the 1992 United Nations Framework Convention on Climate Change (UNFCCC) and the 2015 Paris Agreement by placing undue burdens on exported products. The Proposal states that "[t]is measure will be designed to comply with the World Trade Organization rules and other international obligations of the EU" (page 1). It does not set out the reasons as to how and why the measures proposed are compatible with international obligations incurred by the European Union. The assessment is limited to compatibility with EU law and principles.

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1 Cf. KPMG, Impact of the EU's Carbon Border Adjustment Mechanism (2022), including amendments proposed by Parliament and Council.

2 Laura Basagni, Peter Chase, The Unresolved Trade Problem of Paris – and How Glasgow can Help (German Marshall Fund 2021). Russia, Ukraine, Turkey, Brazil and Mozambique are reported to be most affected by the measure at this stage.

4. This Annex briefly examines issues of legal compatibility of CBAM with the UNFCCC and the Paris Agreement, as well as subsequent instruments adopted by the Contracting Parties. Carbon-leakage and CBMAs are not directly addressed by these instruments, and none of the provisions sets out a framework or specific provisions to which CBAMs are required to comply with. The literature on CBAMs only recently deals with the UNFCCC and the Paris Agreement.[3] Other than WTO law, the two instruments are mainly characterized by programmatic language short of specific rights and obligations. Moreover, there is no direct linkage to trade instruments and tools except for qualifying unilateral measures in Art. 3.5 UNFCCC and for considering and cooperating of response measures under Art. 4.13 of the Paris Agreement. An examination therefore is essentially limited to squaring CBAMs with the basic principles and components of the UNFCCC and the Paris Agreement. The relationship to WTO law is taken up in Annex I.

II. Climate Change: A Common Concern of Humankind

A. International Law

5. The 1992 United Nations Framework Convention on Climate Change recognises it its preamble at the very outset that climate change is a common concern of humankind:

> *Acknowledging* that change in the Earth's climate and its adverse effects are a common concern of humankind
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> The Paris Agreement, its preamble, further elaborates on common concern and states:
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> *Acknowledging* that climate change is a common concern of humankind, Parties should, when taking action to address climate change, respect, promote and consider their respective obligations on human rights, the right to health, the rights of indigenous peoples, local communities, migrants, children, persons with disabilities and people in vulnerable situations and the right to development, as well as gender equality, empowerment of woman and international equity.

6. Recourse to climate change as a common concern of humankind primarily states that it is a shared and common problem. It can only be resolved in cooperation. No country alone is in a position to tackle the problem on its own. Vice-versa, and importantly, efforts made are to the benefit of all humankind, independently of the location of production or consumption. These two outstanding feature characterise a common concern of humankind. The Paris Agreement extended the concept to include many social angles. Countries should consider them in shaping their policies in a sustainable manner. While common concern is recognised and restated in the 2021 COP 26 Glasgow Climate Pact (Preamble para. 3) and the 2022 COP 27 Sharm el Sheik Implementation Plan (Preamble, para 5), it has not evolved into an operational concept in state practice of operational legal impact. Nor has it been invoked and used in the case law of international court and tribunals, so far. The literature mainly relates the

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[3] Gracia Marin Duràn, Carbon Border Adjustments: Ensuring Compatibility with the International Climate and Trade Regimes (University College London 2022); Reinhard Quick, Can Paris Strike Back? On the Paris Agreement's Inability to cope with unilateral trade-related carbon measures such as the European Commission's CBAM Proposal, Festschrift Marco Bronckers, forthcoming 2023 (on file with authors); cf also Reinhard Quick, Carbon Border Adjustment: A dissenting view on its alleged GATT-compatibility, Zeitschrift für Europarechtliche Studien 551 (2020); Aaron Crosbey, Counting carbon: The implications of border carbon adjustments on developing countries (Hinrich Foundation 2021.

concept to the doctrine of shared interests, the idea of public trust, stewardship, global commons and intergenerational equity.[4] Recent research and doctrine proposes to understand common concern of humankind as an emerging legal principle. It obliges states to cooperate, to do their homework and to comply with goals and policies set out internationally and domestically based on commitments made. It addresses the problem of free riding and provides for the possibility of unilateral measures and policies having extraterritorial reach.[5] In the absence of internationally agreed carbon pricing, CBAMs therefore correspond to the principle of common concern. The unilateral measure navigates to promote sustainable modes of protection in completing the domestic emission trading system (ETS).

7. Despite recognising climate change as a common concern of humankind, the UNFCCC and the Paris Agreement do not oblige members to jointly develop policies of climate change mitigation and adaption. Duties to cooperate under the agreements are essentially limited to finance, transfer of technologies and knowhow. The philosophy essentially is one of unilateral measures and nationally defined contributions (NDCs). Sovereignty prevailed. Article 6 of the Paris Agreement recognises the possibility of voluntary cooperation in the implementation of their nationally defined contributions, and Article 6(2) provides:

> 2. Parties shall, where engaging on a voluntary basis in cooperative approaches that involve the use of internationally transferred mitigation outcomes towards nationally determined contributions, promote sustainable development and ensure environmental integrity and transparency, including in governance, and shall apply robust accounting to ensure, inter alia, the avoidance of double counting, consistent with guidance adopted the Conference of the Parties serving the meeting of the Parties to this Agreement.

B. The EU CBAM Regulation

8. The proposed CBAM regulation does not mention climate change as a common concern of humankind. It refers in the Ingress para 2 to the UNFCCC and the Paris Agreement in support of the goal to limit global warming to 1.5^0 C above pre-industrial levels. It is a unilateral measure regulating the importation of goods into the internal market. It does not fall under the ambit of Article 6 Paris Agreement. Third parties and international agreements are not addressed in its operational provisions, except for trade in electricity in Article 2 (see also Annex II B of the Regulation). Given the non-material nature of electricity, special rules for third countries participating in the internal market and market coupling were necessary. There are no provisions relating to the conclusions of international agreements in the operational part. However, para 54 and 55 of the ingress express the willingness of the European Union to international cooperation and to support for developing countries affected by the measure:

> Para. 54 Ingress of the Regulation states:

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4 Jutta Brunnée, Common Areas, Common Heritage and Common Concerns, in Daniel Bodansky, Jutta Brunnée and E Hay, The Oxford Handbook of International Environmental Law 550-573 (Oxford University Press 2007); David French, Common Concern, Common Heritage and other Global(ising) Concepts: Rhetorical Devices, Legal Principles or Fundamental Challenge?, in Michael Bowman, Peter Davies, Edward Goodwin (eds.), Research Handbook on Biodiversity and Law 334-360 (Edward Elgar 2016).

5 Thomas Cottier, The Principle of Common Concern of Humankind, in: Thomas Cottier and Zaker Ahmad (eds.), the Prospects of Common Concern of Humankind in International Law 3-91 (Cambridge: Cambridge University Press 2021).

> The Commission should strive to engage in an even handed manner and in line with the international obligations of the EU, with the third countries whose trade to the EU is affected by this Regulation, to explore the possibilities of dialogue and cooperation with regard to the implementation of specific elements of the Mechanism set out [in] this Regulation and related implementing acts. It should also explore possibilities for concluding agreements to take into account their carbon pricing mechanism.
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> Para 55 Ingress of the Regulation states:
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> As the CBAM aims to encourage cleaner production processes, the EU stands ready to work with low and middle-income countries towards the decarbonisation of their manufacturing industries. Moreover, the Union should support less developed countries with necessary technical assistance in order to facilitate their adaptation to the new obligations established by this regulation.

9. The prospects of enhanced international cooperation in the field respond to the prospects of common concern of humankind. As long as such agreements are missing, and a global carbon price has not been agreed which all members of the UNFCC and the Paris Agreement would globally apply, or within a plurilateral carbon-club agreement, across the board, CBAM as a unilateral measure deploying extraterritorial reach is compatible with the emerging principle of common concern. Unilateral policies contribute to achieving the overall goal of abatement of CO_2 emission towards the stated goal of limiting warming to 1.5^0 C. Given the market size of the EU, it may eventually trigger and support the achievement of a globally agreed system for CBAMs which, at this stage, is not in reach beyond talks in the G7. At the same time, common concern as expressed the preamble also obliges unilateral measures to be adopted in a manner compatible with the interests of vulnerable strata of society and of countries. It implies that measures adopted need to be socially compatible and comply with all the three elements of the principle of sustainability (economic, ecological and social).

10. The compatibility of CBAM with the precepts of common concern strongly depends upon the scope of the measure. The EU proposal extends the measure to a limited number of goods and to direct emissions. It does not include agricultural products. The proposal includes in Annex I cement, electricity, fertilisers, iron and steel, and aluminium. Most of these products originate in industrialised and emerging economies. The extension of CBAMs to indirect emission and a much larger group of products would affect many more countries and thus require under common concern proactive policies to deter and avoid socially detrimental effects in exporting countries.

III. Common but Differentiated Responsibilities

11. The CBAM, as proposed by the EU, clearly focuses on effective reduction of CO_2 emission. It flanks domestic Carbon emission trading and seeks to avoid carbon leakage that undermines abatement goals. It applies across the board of all imported products, independently of their origin. Conceptually it does not make a difference between industrialised countries, emerging economies and developing countries. The 1992 UNFCCC was based upon the philosophy that the responsibility to abate greenhouse gas lies with industrialised

countries as they had caused the increases and thus the problem.[6] Article 3 paras. 1 and 2 state:

> 1. The Parties should protect the climate system for the benefit of present and future generations of humankind, on the basis of equity, and in accordance with their common but differentiated responsibilities and respective capabilities. Accordingly, the developed country Parties should take the lead in combating climate change and the adverse effects thereof.
> 2. The specific needs and special circumstances of developing country Parties, especially those that are particularly vulnerable to the adverse effects of climate change, and of those Parties, especially developing country Parties, that would have to bear a disproportionate or abnormal burden under the Convention, should be given full consideration.

12. Annex I listed industrialised countries accordingly. Developing countries, faced with the impact of climate change, are entitled to support in the process of adaptation. The 2015 Paris Agreement extended basic obligations to all Members and thus the international community at large. The price paid for the extension was the limitation to unilateral and formally non-binding nationally determined commitments (NDCs) to be made and notified. The principle of common but differentiated responsibilities was maintained and is expressed in Article 2 para. 2:

> 2. The Agreement will be implemented to reflect equity and the principle of common but differentiated responsibilities and respective capabilities, in the light of different national circumstances.

13. Leadership in climate change mitigation thus rests with industrialised countries and emerging economies. The agreement encourages unilateral commitments. It inherently supports unilateral measures to the extent that international cooperation is not able to achieve the goals of limiting global warming to 1.5^0 C in time. The introduction of emission trading and, as a corollary, CBAMs in principle responds to the enhanced responsibility of industrialised countries. The principle of common responsibility implies that developing countries are obliged to support the effort in principle and support the effort to deter and avoid carbon leakage, undermining the1.5^0 C commonly adopted and supported. In principle, CBAM is in line with this obligation of the UNFCCC and Paris Agreement. Objections may be raised on modalities whether the system sufficiently respects the principle of differentiated responsibility, taking into account the scope and extension of the measure.

14. It is an open question to what extent CBAM affects developing countries.[7] Much depends upon the scope of the measure, i.e. the number and type of products included, and whether it will extend to indirect emission inherent to traded goods. The Commission will collect data with a view to extent the system to other sectors and indirect emissions (Ingress para 52). The extension, reinforced by Parliament to gradually extent the system to indirect emissions with a view to enhance its effectivity needs to correlate with financial support and enhanced efforts at dissemination and transfer of knowledge and sustainable technologies under the UNFCCC and the Paris Agreement. Developing countries and industries subject to CBAMs are entitled to support in adjusting process and production methods with a view to meet emissions standards of the importing jurisdiction.

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6 See generally Christopher D. Stone, Common but Differentiated Responsibilities in International Law, 98 American Journal of International Law 276-301 (2004).

7 See Crosbey note 3.

15. CBAM qualifies under the Paris Agreement as a response measure. The decision CP 21 recognises the specific needs and concerns of developing country "arising from the impact of the implementation of response measures" and refers to this effect to previous decisions 5/CP 7, 1CP.10, 1/CP.16 and 8/CP.17. The Forum on the Impact of the Implementation and Response Measures is obliged to enhance cooperation in understanding the impact of implementation measures, such as CBAM (para. 34). The Ad Hoc Working Group on the Paris Agreement, inter alia, is required to provide information on the social and economic impact of response measures (para. 95 lit. f). Article 4 para. 13 in particular requires Parties to "take into consideration in the implementation of this Agreement the concerns of Parties with economies most affected by the impacts of the response measures, particularly developing countries". These obligations clearly require the EU as well as Switzerland in contemplating CBAM to address the concerns of countries most affected by the measure.

16. Based upon the EU proposal, such concerns have not been addressed. CBAM applies across the board and does not address how such concerns will be taken into account in the operation of the system. In that respect, the proposal does not live up to the obligations under the Paris Agreement, in particular the principle of common but differentiated responsibility. The literature shares this view.[8]

IV. Unilateral Measures

17. Both UNFCCC and the Paris Agreement allow for unilateral measures in addressing climate change mitigation and adaption. This is inherent to the concept of nationally determined commitments (NDCs). Art. 3.5 of the UNFCC qualifies such measures as follows:

> The Parties should cooperate to promote a supportive and open international economic system that would lead to sustainable economic growth and development in all Parties, particularly developing country Parties, thus enabling them to better address the problems of climate change. Measures taken to combat climate change, including unilateral ones, should constitute a means of arbitrary or unjustifiable discrimination of disguised restrictions on international trade.

18. The provision both entails and obligation to cooperate, but also allows for unilateral measures qualified in terms borrowed from the chapeau of Article XX GATT which applies these qualifiers to countries where the same conditions prevail (see Annex I). It is unclear whether Art. 3.5 UNFCCC imports here the principle of common but differential responsibility or rather the disciplines of GATT that per se do not distinguish as such between developing and developed countries. Rather, Article the chapeau of XX GATT assures that measures are reasonable and do not treat comparable countries in a different manner. We return to this in Annex II.

V. Financial Support

19. Financial support by industrialised countries amounts to the prime obligation under the principle of common and differentiated responsibility. Taking into account the historical causation of climate change induced by 19th and 20th Century industrialization, developed countries are obliged to provide financial support to developing countries. The UNFCCC essen-

[8] Supra note 3.

tially provides for the Global Fund in Article 11 (Financial Mechanism) and obliges developed countries in Article 1 para. 5 to fund, as appropriate the transfer of, and access to, environmentally sound technologies. Article 9 of the Paris Agreement states:

> 1. Developed country Parties shall provide financial resources to assist developing country Parties with respect to both mitigation and adaptation in continuation of their existing obligations under the Convention.

20. The agreements do not exclusively define the modes of funding. It may take place through ODA which depends upon budgetary allocation and so far has not reached pledged goals. The Glasgow Climate Pact places funding at its centre, and stresses large scale contributions to be made (para. 14-21, 40-60). There is no explicit obligation in these agreements to link funding to market mechanisms and revenues, and they are not mentioned in the 2021 Glasgow Pact. Thus, there is no legal obligation to establish a formal linkage between CBAMs and obligations to support and fund efforts at mitigation and adaptation in developing countries. The 2022 COP 27 did not made progress in emission reduction standards and funding of mitigation measures, in particular on the part of emerging economies, in particular Brazil, China, India and Saudi Arabia. The emphasis was placed on measures relating to loss and damages incurred by the global South. A new global fund was in principle adopted by the Sharm el-Sheik Implementation Plan para. 24 and decisions -/CP27 and -/ CMA.4, adopted in November 20, 2022. It does not relate to mitigation measures.

21. It is evident that the political acceptability of CBAMs by those affected is greatly enhanced to the extent that proceeds are used to comply with the obligations under Article 9 of the Paris Agreement. It may be argued that unlinked proceeds of CBAMs can be annually ear marked and used through budgetary processes to support countries in greater need in adapting to climate change. Thus, the allocation to the general budget and a commitment to use proceeds for climate change mitigation and adaptation in less developed countries is more appropriate to comply with the unilateral promise made in Ingress para 54 and 55 above. We note, however, that these proceeds are directly burdened upon products from developing countries and the costs, indirectly, are borne by them in losing a comparative advantage and market access. They are not concessionary financial contributions in the meaning of Article 9 Paris Agreement. From that perspective, it seems reasonable to establish a transparent, regular linkage and use of proceeds to support the transition of exporting industries affected by the imposition of CBAMs. This would also need to be considered if CBAMs are levied in the form of carbon tariffs.

VI. Dissemination of Knowledge and Sustainable Technologies and Capacity Building

22. Dissemination of knowledge and sustainable technology is at the heart of the UNFCCC and the Paris Agreement and subsequent COP decisions. The UNFCCC consistently emphasises the need for transfer of technology and expertise in its provisions [Art. 11(1), Article 4(3), (7) (8) (9)]. Article 4(5) states an explicit obligation of developed countries to this effect:

> 5. The developed country Parties and other developed Parties included in Annex II shall take all practicable steps to promote, facilitate and finance, as appropriate, the transfer of, or access to, environmentally sound technologies and know-how to other Parties, particularly developing country Parties, to enable them to implement the provisions of the Convention. In this process, the developed country Parties shall support

the development and enhancement of endogenous capacities and technologies of developing country Parties. Other Parties and organisations in a position to do so may also assist in facilitating the transfer of such technologies.

23. The Paris Agreement confirms the mandatory commitment in Article 10 and establishes a Technology Mechanism and a technology framework:

1. Parties share a long-term vision on the importance of fully realizing technology development and transfer in order to improve resilience to climate change and to reduce greenhouse gas emissions.
2. Parties, noting the importance of technology for the implementation of mitigation and adaptation actions under this Agreement and recognizing existing technology deployment and dissemination efforts, shall strengthen cooperative action on technology development and transfer.
3. The Technology Mechanism established under this Convention [by COP 2010] shall serve this Agreement.
4. A technology framework is hereby established to provide overarching guidance to the work of the Technology Mechanism in promoting and facilitating enhanced action on technology development and transfer in order to support the implementation of this Agreement, in pursuit of the long-term vision referred to in paragraph 1 of this Article.

   Article 11 stresses the importance of capacity building:

5. All Parties should cooperate to enhance the capacity of developing countries to implement this Agreement. Developed country Parties should enhance support for capacity building actions in developing country Parties.

24. The Technology Mechanism consists of two bodies. The Technology Executive Committee (TEC) and the Climate Technology Centre and Network (CTNS). It does not seem that these bodies so far have dealt with CBAM. Para 22-36 of the Glasgow Climate Pact of CP 26 adopted on November 13, 2021, and para. 41- 43 of the Sharm el-Sheik Implementation Plan of COP 27, adopted November 20, 2022, reiterate the call for transfer of technology and finance but do not address issues related to border tax adjustment. Since the UNFCCC and the Paris Agreement do not address trade and border adjustment, no specific obligations to transfer technology and expertise exist in the Agreement and subsequent instruments and decisions.

The EU CBAM proposal does not address transfer of technology and capacity building with developing countries affected by the measure in its provisions beyond the Ingress. The UNFCCC and the Paris Agreement does not oblige to do so. Yet, again, it is obvious that CBAM can be used to comply with the basic obligation under Article 10 para. 2 to contribute to strengthening cooperation with developing countries affected by the measure and to enable industries to adopt sustainable production methods by which they are enabled to avoid the measure imposed.[9]

[9] See Zaker Ahmad, WTO Law and Trade Policy Reform for Low-Carbon Technology Diffusion: Common Concern of Humankind, Carbon Pricing and Export Credit Support, Leiden: Brill 2021; ibid., Trade-Related Measures to Spread Low-Carbon Technologies: A Common Concern-Based Approach, in Thomas Cottier and Zaker Ahmad (eds.) note 3 p. 95-152.

VII. Other Options

25. Common but differential responsibilities is not limited to financial support and transfer of technology. Studying options for the UK, modes of special and differential treatment (S&D) could be examined for the treatment of developing countries entitled under the UNFCCC and the Paris Agreement. In a comprehensive and important study, the UK Trade Policy Observatory and the Centre of Inclusive Trade set out a number of basic options next to refunding and transfer of technology with a view to realise differentiated and thus reduced responsibility for developing countries affected by Border Carbon Adjustment (BCA):[10]

1. Exempt LDCs from BCAs;

2. Exempt LDCs from mandatory minimum standards;

3. Do not exempt any country on basis of level of development;

4. Direct some or all of BCA revenues to developing countries; or

5. Offer capacity-building support for adoption.

26. While Option 3 ignores differentiation, and options 4 and 5 correspond to the findings under the UNFCC and the Paris Agreement, options 1 to 3 will need to be assessed in terms of WTO law and how it can be reconciled with the UNFCC and the Paris Agreement, partly aligning to the General System of Preferences (GSP). Exemptions, however, will retard structural adjustment in developing countries and reproduce some of the detrimental effects of special and differential treatment. Without incentives to adjust, carbon emissions will not be reduced in the manufacturing process and the common concern is not effectively addressed. Funding and technology transfer thus remain preferred options in our view which can be aligned with the linkage to emission trading, as in the case of the EU proposal on CBAM.

VIII. Avoidance of Double Counting of Contribution to Emission Reduction

27. The UNFCCC and the Paris Agreement do not state in the logic of nationally determined contributions a general prohibition of double counting of contributions to emission reduction. A prohibition is provided for in Article 6 in the context of cooperation (above section II, see also section III para. 15 on Decisions to give effect to the Agreement [paras 37, 93(f), 107 and 108]. Absent a bilateral or plurilateral agreement, Parties are not yet obliged to avoid double counting of contributions. The proposed CBAM regulation unilaterally recognises the need to avoid double counting. Importers are allowed to deduct actual payments for a carbon-price imposed in the country of production and exportation.

Article 9 of the Regulation states:

1. All authorised declarant may claim in its CBAM declaration a reduction in the number of CBAM certificates to be surrendered in order for the carbon price paid in the country of origin for the declared embedded emission to be taken into account.

2. The authorised declarant shall record of the documentation, certified by an independent person, required to demonstrate that the declared embedded emissions were subject to a carbon price in the country of origin of the goods and keep evidence of the

[10] Emily Lydgate, L. Alan Winters, Peter Dodd, Camilla Jensen, Guillermo Larbalestier, Chloe Anthony and Camille Vallier, Trade policies and emission reductions: establishing and assessing Options 67 UKTO/CITP 29 June 2022).

proof of the actual payment for that carbon price which should not have been subject an export rebate or any other form of compensation on exportation.

28. The CBAM regulation thus allows to deduct financial contributions made in the exporting country [see also Article 6 para 2(c)]. The Commission Staff Working documents confirm that "In options 1-5, the method to establish the embedded emissions of imported products will have to be designed to avoid double counting" (p. 55).

29. The unilateral exclusion of double counting is limited to financial contributions and does not take into account efforts at abatement through regulations or other than financial means. Avoidance of double counting in the sense of Art. 6 Paris Agreement extending beyond financial contributions can be taken up in bilateral cooperation agreements with individual countries. To this effect, there is no incompatibility of CBAM with the Paris Agreement.

IX. Conclusions

A. CBAM Regulation in line with goals of UNFCCC and Paris Agreement

30. The UNFCCC and the Paris Agreement both do not explicitly address levies imposed upon importation of products. They allow for unilateral measures, and CBAMs clearly promote and advance the goals of these agreements as they deter carbon leakage and encourage exporting industries to adjust process and production methods. In the absence of internationally agreed standards, unilateral measures imposed – second best – are in line with both the spirit and terms of the Agreements. They address a common concern of humankind and bring about progress in abating greenhouse gases.

B. CBAM falls short of obligations on support for Developing Countries

31. The UNFCC and the Paris Agreement, however, oblige members to take into account the effects on unilateral measures on other countries, in particular developing countries. To the extent that their exports are affected, assistance by means of funding and transfer of knowledge and technology must be provided under these agreements, allowing adapting production and processing methods. Such support is part of addressing the common concern. It is in the interest of both the importing and the exporting country to reduce greenhouse gas emissions.

32. The purpose of CBAM is avoiding carbon leakage, but also to encourage producers abroad to restructure production processes with a view to reduce greenhouse gas emissions. The second function is not sufficiently materialised in the proposed regulation. Structural adjustment is limited to the impact of extraterritorial effects of EU. The proceeds fall into the general budget of the EU and are not earmarked for structural adjustment of foreign exporting industries. The Regulation does not provide a legal basis for pro-active support and dissemination of sustainable technology. Unless provided for in a different instrument, it falls short of the obligations and expectations created for developing countries by the UNFCCC and the Paris Agreement. The shortcoming explains much of the resistance to CBAM will materialise in the context of international trade disputes.

33. In this respect, the EU CBAM Regulation falls short of the UNFCCC and Paris Agreement. It is designed as an internal market instrument complementing the domestic emission trading system, while strongly affecting imports and third countries and economies. Proceeds of the system pertain to the general budget and can be used for any purpose. While funding and transfer of technology are addressed in preambular terms, no operative provisions exist to this effect.

C. Inclusion of funding and transfer of technology recommended

34. It is therefore appropriate to include, beyond preambular language, funding mechanism and dissemination of knowledge and technology to low income developing countries with a view to meet obligations incurred under the UNFCCC and the Paris Agreement under the principle of common but differentiated responsibility. The regulation of CBAMs should define, independently of the form of the levy, the obligation to purchase certificates and corresponding proceeds to be an earmarked levy, defined and limited to a specific purpose. Proceeds should be returned by law to foster structural adjustment and clean modes of production in the industries concerned. Since climate change is a common concern of humankind, these proceeds should be returned to exporting industries in support of structural adjustment. They will directly benefit all consumers and citizens alike.

35. Under the UNFCCC and the Paris Agreement, low-income countries and developing countries are legally entitled to support. Such entitlement does not extend to industrialised countries and emerging economies under these agreements. The problem is that neither in public international law nor in treaty law are these categories clearly defined except for the group of least-developed countries. The CBAM regulation therefore should define criteria for entitlement of industries in countries concerned.

36. In defining allocations, much will depend upon the trade flows of goods falling under the regulation. Many of the exports originate in industrialised countries not entitled under the UNFCCC and the Paris Agreement to funding and transfer of technology. Direct entitlement of exporting industries affected would channel most of the proceeds to industrialised countries and reduce the amount of resources available to those entitled in international law. Moreover, it is unclear to what extent proceeds will be sufficient to foster structural adjustment in exporting industries of countries entitled to support. Moreover, it will depend upon markets who actually bears the additional costs by the obligation to buy certificates. It may be the domestic consumer, the importer or the exporter in adjusting pricing. More research is required here. Yet, whoever pays, it is evident that conditions of competition and market access of exporting industries subject to CBAM obligations are adversely affected compared to previous levels of market access determined to levels of tariff imposition and possibly import quota regulations.

37. Given these uncertainties, it may be best to pool the proceeds and earmark them for structural adjustment support in countries entitled under the UNFCCC and the Paris Accord. Likewise, in parallel, proceeds of selling ETS certificates to domestic industries and thus removing the subsidy of free allowances should be returned to the industry in support of structural adjustment. A linkage should be established in parallel to the internal system of emission trading. To the extent that emission certificates no longer are granted on a concessionary basis and thus as subsidy, proceeds from the acquisition of proceedings by polluting industries should be used to fund structural adjustment with a view to achieve climate neutral means of production in the industry. Revenues thus should be returned to the industry and thus earmarked.

38. Dissemination of knowledge and transfer of sustainable technology should not only be encouraged, but actually supported by using CBAM proceeds (and other means) to fund licensing of technology from domestic industries to industries in eligible countries. While the system of voluntary licensing of patents is feasible and effective where financial means are sufficiently available, such transfers depend on support where they are insufficient. Recourse to compulsory licensing, possible under the TRIPS Agreement of the WTO, does not allow access to undisclosed information and technical assistance crucial in the process of structural adjustment towards new and sustainable modes of production.

39. Earmarking proceeds both the ETS and CBAM revenues is in line with the purpose and goals of the UNFCCC and the Paris Agreement. Annex I explains that such measures are compatible with WTO law. It would greatly enhance the political acceptability of the system abroad and deter fears of economic protectionism.

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