From Unilateral Border Carbon Adjustments to Climate Clubs?

While the EU’s proposed CBAM would mark the first time any jurisdiction adopts a BCA targeting foreign goods, it is unlikely to be the last. In Canada, the federal government launched a consultation process to consider...
how a BCA could help the country meet its climate targets. Similarly, the UK Parliament’s Environmental Audit Committee opened an inquiry into BCAs. Meanwhile, in the United States, Senator Christopher A. Coons and Representative Scott H. Peters introduced a bill that would impose a fee on imports of certain carbon-intensive products based on the “domestic environmental cost” incurred by U.S. producers under a portfolio of climate policies. More recently, Senator Sheldon Whitehouse has introduced a bill that would impose a BCA on a range of imported goods based on a levy domestic manufacturers would pay for emissions that exceed the industry average.

Although designed as a unilateral measure, the EU’s CBAM could offer a foundation for international cooperation among like-minded jurisdictions. Recent developments lend support to such a possibility. On the eve of the Glasgow Climate Conference in November 2021, the United States and the EU issued a joint statement on trade in steel and aluminum, an area where the two trading partners have clashed in the past. Under the deal, both sides agreed to expand market access and suspend ongoing trade disputes over steel and aluminum tariffs at the World Trade Organization (WTO), while also launching negotiations on a Global Arrangement on Sustainable Steel and Aluminum scheduled to conclude by 2024. This agreement would, inter alia, commit participants to “restrict market access for non-participants that do not meet standards for low-carbon intensity.” Another suggestion for international cooperation entailing a possible BCA has come from German Federal Chancellor Olaf Scholz, who expressed an interest in forming an international “climate club” during Germany’s Group of Seven (G7) Presidency in 2022. While the G7 Statement on Climate Club adopted in June 2022 does not specifically mention BCAs, it commits the G7 to the establishment of “an open and cooperative international Climate Club” by the end of 2022, and expressly mentions “countering carbon leakage at the international level” as one of its goals.

While international cooperation on BCAs is thus emerging as a policy option on both sides of the Atlantic, it is less evident what shape such cooperation might take. Some calls for cooperation involving BCAs have invoked the concept of a “climate club” without offering a clear definition of the concept. As evidenced by the vision set out by G7, the notion of a “club” is typically used in a much broader sense than that proposed in economic theory, where it entails an excludable “club good”—that is, a benefit to which only members have access—as well as penalties for non-compliant members and non-members.

Several ideal types of clubs can be distinguished: normative clubs, under which like-minded members commit to achieving certain climate policy goals; bargaining clubs to enable more efficient negotiations of objectives, targets, and policies among major powers; and transformational clubs, which set legally binding rules for members and offer incentives for participation and compliance in the form of club goods and sanctioning. While the latter best

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4 See Gov’t of Canada, Consultation on Border Carbon Adjustments (2021).
5 See UK Parliament, Call for Evidence.
6 Fair, Affordable, Innovative, and Resilient Transition and Competition Act, S.2378, 117th Cong. (2021).
7 S.4355, 117th Cong. (2022).
8 Steel and Aluminum: U.S.-EU Joint Statement (Oct. 31, 2021).
9 Id.
10 Steps Towards an Alliance for Climate, Competitiveness and Industry – Building Blocks of a Cooperative and Open Climate Club, at 5 (Aug. 2021).
11 G7 Statement on Climate Club (June 28, 2022).
12 Id.
13 James M. Buchanan, An Economic Theory of Clubs, 31 Economica 1 (1965).
14 Robert Falkner, Naghmeh Nasiritousi & Gunilla Reischl, Climate Clubs: Politically Feasible and Desirable?, 22 Clim. Pol’y 480 (2022).
describes the prominent call for a “climate club” articulated by economist William Nordhaus,\textsuperscript{15} the “club” designation is still often used to refer to any form of international climate cooperation with less than universal participation.

Irrespective of whether it merits the label of a “club,” cooperation on BCAs between two or more trading partners will have to address three main questions. First, what legal form should international cooperation on BCAs take? International law in “her infinite variety” comprises a range of possible instruments,\textsuperscript{16} each of which can generate varying legal effects. Closely related to form is a second question, namely: through what forum—existing or new—can and should such cooperation be pursued? And third, what would constitute the substance of such cooperation, both in procedural and material terms? While not offering definitive answers to these questions, we consider the landscape of options policymakers will need to navigate.

\textit{Form}

In pursuing cooperation on BCAs, jurisdictions have the option of enshrining such cooperation in a legally binding treaty or in more informal arrangements without binding status.\textsuperscript{17} A formal treaty would signal a strong commitment, as most states require domestic ratification, usually involving approval by a legislature. Even in the absence of a formal enforcement mechanism, legally binding treaty obligations may exert a “compliance pull,” for instance by making non-compliance less attractive due to the reputational damage caused. Treaties also tend to be more amenable to enforcement in domestic legal orders.\textsuperscript{18} While offering greater legal certainty, however, treaties are more cumbersome to negotiate and ratify as compared to informal agreements. Pursuing a treaty containing legally binding provisions may also make it more challenging to attract participation by states, and may altogether rule out participation of subnational jurisdictions, such as provinces or municipalities.

By contrast, more informal arrangements—such as a memorandum of understanding—would not only avoid the foregoing drawbacks but could also allow for greater flexibility in the face of evolving circumstances.\textsuperscript{19} While details remain sparse, the Global Arrangement on Sustainable Steel and Aluminum, for instance, is likely to be non-binding in nature. Given that BCAs are only beginning to see concrete elaboration, such flexibility appears particularly desirable at this early stage, enabling international cooperation to better adjust to unfolding political dynamics at the domestic and international level.

Even if states agree on a legally binding treaty, not all provisions need to be binding: international cooperation on BCAs could include a combination of non-binding objectives and principles as well as binding procedural obligations. Such binding obligations would offer greater legal certainty, but they would likewise be more challenging to negotiate and, depending on their substance, may require ratification at the domestic level.

\textit{Forum}

Although international cooperation on BCAs could emerge within its own political and institutional context, as the Global Arrangement on Sustainable Steel and Aluminum illustrates, embedding it within an existing forum

\textsuperscript{15} William D. Nordhaus, \textit{Climate Clubs: Overcoming Free-Riding in International Climate Policy}, 105 Am. Econ. Rev. 1339 (2015).

\textsuperscript{16} R.R. Baxter, \textit{International Law in “Her Infinite Variety”}, 29 Int’l & Comp. L.Q. 549 (1980).

\textsuperscript{17} Note, however, that the legal form of BCA cooperation is distinct from the legal form of the actual BCAs, which are likely to be implemented through binding domestic law.

\textsuperscript{18} Daniel Bodansky, \textit{Legally Binding Versus Non-legally Binding Instruments}, in \textit{Towards a Workable and Effective Climate Regime} 160–63 (Scott Barrett, Carlo Carraro, & Jaime de Melo eds., 2015).

\textsuperscript{19} Charles Lipson, \textit{Why Are Some International Agreements Informal?}, 45 Int’l Org. 495 (1991).
could offer benefits. Not only would it provide a setting for the political negotiations preceding cooperation, but it could also afford an institutional “home” with existing administrative and financial resources. Different options exist to institutionalize cooperation on BCAs, each with different implications for the relevant procedures, actors, and political dynamics.

One such option is cooperation under the international climate regime. Cooperation on BCAs could be framed as promoting the implementation of parties’ nationally determined contributions under the Paris Agreement. Parties could negotiate the terms of cooperation through existing processes, such as the annual climate summits, and build on operational support from the standing bodies of the international climate regime.

Another international regime that could provide a forum for cooperation is the WTO, under whose auspices members could initiate dialogue through relevant bodies such as the Committee on Trade and Environment. Indeed, BCAs are expected to feature in the Trade and Environmental Sustainability Structured Discussions, an initiative recently launched by a subset of WTO members. Given political realities, however, options for more substantive engagement under the WTO regime—such as plurilateral trade agreements or a customs union—are unlikely to offer a basis for cooperation on divisive trade-restrictive measures such as BCAs.

“Minilateral” approaches outside a multilateral regime may therefore hold greater promise, although these could again evolve within the confines of an existing institution whose structures and processes would facilitate the necessary dialogue. Germany, for instance, has endorsed discussing its proposed “climate club” within the G7 and, subsequently, the Group of Twenty. Both groups of countries are informal gatherings without a mandate to adopt binding agreements, but they can serve as a vehicle for signaling political commitment.

By contrast, the Organisation for Economic Co-operation and Development, which has recently expressed interest in fostering cooperative engagement around BCAs, represents a type of formal organization that possesses a sizeable career staff and abundant technical and epistemic resources, all of which it could leverage to foster cooperation on BCAs.

Finally, cooperation on BCAs could occur through bilateral arrangements. The proposed CBAM, for instance, envisions the ability of the EU to “conclude agreements with third countries with a view to take account of carbon pricing mechanisms in these countries.” Although the geographic scope of such bilateral cooperation would be limited, it could provide the nucleus for expanded BCA cooperation over time—for instance through inclusion in regional agreements, such as the Agreement on Climate Change, Trade and Sustainability launched in 2019 by New Zealand, Costa Rica, Fiji, Iceland, Norway, and Switzerland.

Substance

While initiatives in other issue areas offer insight into the possible form and forum of cooperation on BCAs, the lack of relevant precedent makes it less obvious what such cooperation could entail on substance. Existing proposals involving cooperation on BCAs are highly heterogenous, ranging from informal engagement on best practices to deep political and economic integration that includes some form of BCA. What these proposals mostly have in common, however, is that they set out both procedural and material elements, making this distinction a useful starting point.

20 For a potential template for such discussions, see Report of the GATT Working Party on Border Tax Adjustments, GATT Doc. L/3464 (Dec. 2, 1970).
21 Matthew C. Porterfield, Climate Clubs: Key Design & WTO Compliance Issues (Apr. 2022).
22 Susanne Droegge & Marian Feist, The G7 Summit: Advancing International Climate Cooperation? (May 2022).
23 Sam Fleming & Chris Giles, OECD Seeks Global Plan for Carbon Prices to Avoid Trade Wars, FIN. TIMES (Sept. 13, 2021).
24 Eur. Comm’n, supra note 2, Art. 2(12).
Of the two, *procedural* cooperation can offer a first step toward engagement even when support for material commitments is lacking. Any initiative to foster cooperation on BCA design and implementation is likely to involve, for instance, one or more procedures to facilitate engagement between participating jurisdictions. Such procedures can be as elementary as periodic consultations—which can take the form of workshops, staff meetings, or any other recurring exchange of views—as well as a pledge to notify cooperation partners in good faith prior to taking certain actions.

More formal procedures can intensify cooperation by defining clear routines backed by reciprocal expectations. For instance, cooperation partners might commit to reporting obligations and a review of their climate policy progress to enhance mutual transparency and trust. Review procedures could also serve to monitor climate policy efforts or industrial performance in third countries, yielding information useful for calculating BCA levels and determining exemptions. Partners may even agree on a process to settle any ensuing conflicts or disputes.

To assist with routine cooperation tasks and potentially afford some degree of independent oversight, partners could further designate a standing body—new or existing—to serve as a secretariat or technical support unit, in which case they would have to define its mandate and composition, set out operational functions, and allocate commensurate resources. Under the Global Arrangement on Sustainable Steel and Aluminum, for instance, a technical working group is expected to confer on methodologies and facilitate sharing of relevant data.\(^{25}\) In its most formal iteration, an institution could be vested with legal personality and afforded the power to adopt decisions that guide or constrain the activities of cooperation partners, for instance by designing harmonized rules or minimum standards.

Decisions on rules or standards already relate to the second category of substantive cooperation on BCAs—its *material* dimension. Materially, BCA cooperation can again span a range of options, from defining broad aspirational principles to imposing detailed prescriptions on BCA design and implementation. Shallow cooperation could entail an exhortation to adhere to shared objectives, principles, or practices, which would allow partners to align activities without ceding control over the process and content of BCA deployment. To this end, they could agree on a set of shared understandings on, *inter alia:*

- legitimate objectives of BCAs and the circumstances that justify their use;
- recommendations for BCA design and implementation, including for the determination of emissions embedded in traded goods, recognition of climate efforts by trade partners, or revenue use; and
- addressing impacts from BCA implementation on vulnerable countries.\(^{26}\)

Cooperation could be deepened with more specific commitments that narrow the flexibility available to partners—for instance through the adoption of detailed technical methodologies, or through agreement on mutual rights and obligations, such as a reciprocal defense clause to provide legal space for BCAs or a waiver of action related to BCAs under existing dispute resolution mechanisms.\(^{27}\)

In the context of a “climate club,” such material arrangements would also have to encompass the substantive conditions for club membership as well as the attendant benefits, such as avoidance of a BCA, other forms of preferential market access, or financial and technological support. Conditions might include the achievement of a particular level of climate policy ambition, as demonstrated, for instance, by a minimum carbon price.

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\(^{25}\) U.S.-EU Joint Statement, *supra* note 8, at 2.

\(^{26}\) Aaron Cosbey, *Principles and Best Practice in Border Carbon Adjustment: A Modest Proposal* (Sept. 2021); Dave Sawyer & Renaud Gignac, *Border Carbon Adjustments: The Case for a Cooperative, Principles-Based Approach* (Feb. 2022).

\(^{27}\) James Bacchus, *The Case for a WTO Climate Waiver,* CTR. INT'L GOVERNANCE INNOVATION (2017).
Alternatively, cooperation partners could seek to retain flexibility for their domestic climate policies and instead focus on environmental performance.  

Instead of keeping membership open to any trading partners that meet specified conditions, members might even opt for a “closed” club, with participation limited to the initial members based on existing political and economic ties or shared values.

**To Club or Not to Club?**

In setting out different options for cooperation on BCAs, we have argued that the form and substance of such cooperation are closely interrelated. If past cooperation in other issue areas is any guide, BCA cooperation will likely unfold as an evolutionary process, starting with limited geographic and normative scope, and increasing in prescriptiveness and coverage over time. As such, it may transition from a “normative club” to a “transformational club” in the typology of clubs introduced earlier.

This essay has not sought to address the merits of such cooperation. In principle, any cooperation is preferable to unilateral action, as it can avoid a proliferation of heterogeneous or even conflicting approaches, while also averting diplomatic fallout and legal disputes by providing greater transparency and mutual engagement. At the same time, if cooperation on BCAs accelerates the current trend toward expanded use of coercive trade measures to advance domestic political priorities, it will also have to carefully navigate the attendant risks.

While the growing reaction to unintended effects of increasing trade liberalization—such as impacts on workers and their communities, dependence on strategic supply chains, or indeed emissions leakage—is understandable, it should not be a justification for protectionism, nor come at the expense of the least developed countries. Like the German proposal for a “climate club,” cooperation on BCAs will ideally be inclusive and transparent, extending beyond BCAs to focus on benefits such as lowered barriers for clean technology diffusion and expanded access to climate investment.

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28 Todd N. Tucker & Timothy Meyer, *A Green Steel Deal: Toward Pro-Jobs, Pro-Climate Transatlantic Cooperation on Carbon Border Measures* (2021).

29 The degree of formality and depth of cooperation can involve mutual tradeoffs, however. See Kal Raustiala, *Form and Substance in International Agreements*, 99 AJIL 581 (2005).

30 UNCTAD, *A European Union Carbon Border Adjustment Mechanism: Implications for Developing Countries* (July 2021).

31 Leonidas Parousos, et al., *Climate Clubs and the Macro-economic Benefits of International Cooperation on Climate Policy*, 9 Nature Clim. Change 542 (2019).