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Should Australia join the emerging club of carbon trading nations?

Australia's exports risk being hit with environmental charges if it doesn't move quickly in the face of trade mechanisms being considered by climate-progressive nations as they seek to prevent the leakage of jobs and investment to climate laggard nations.

Last week, the UK announced that it would start the process necessary to work out how to set up a Carbon Border Adjustment Mechanism (CBAM) and next week the European Parliament will debate the detail embodied in its proposed CBAM. Expedited implementation and an expansion to around 60 more sectors is under consideration.

Canada is well down the CBAM development pathway and, last year, the US considered introducing a carbon import tax.

The rules that have been governing international trade for many years are under significant challenge.

Anticipating the formation of a club of nations interested in finding a way to prevent the leakage of jobs from climate-progressive to climate-laggard nations, the University of Adelaide's Institute for International Trade (IIT) has released a paper that puts forward ten principles for the development of border adjustment mechanisms.

"By moving first, the EU has gained a massive political advantage." Author of the paper, Professor Mike Young, says: "If the paper's principles are accepted then the EU would need to add at least two new features to its proposal."

The first need is to add an equivalent contribution provision that would exempt the requirement to pay for the cost of purchasing the emission permits that would be necessary if imports of iron ore, steel, cement, fertilizers, aluminium and electricity were produced in the EU.

"Imports from any country that has been reducing emissions as fast, or faster than, the EU should be exempt from the proposed CBAM payment," says Professor Young.

Drawing on Australian experience in the use of Producer Subsidy Equivalents in agriculture as a means to help increase agricultural trade, Professor Young says that the second need is to "shift from a requirement to have the equivalent of a carbon tax to an equivalent pricing arrangement that recognises the impact of regulations and standards on production costs."

"Under the current EU proposal, the impact of Australia's Renewable Energy Targets on production costs would count for nothing. Similarly, a decision to offset carbon emissions would gain zero recognition. The only things that count are direct carbon payments to a government."

As Australia begins the process of re-evaluating its climate change policies, it needs to think carefully about whether or not it wants to join and even play a significant role in shaping the structure of CBAMs. "Time is no longer on Australia's side," says Professor Young.

"At the moment Australia has no carbon tax and no emissions trading system in place. If Australia wishes to avoid the imposition of a carbon tax on its exports, it needs to act quickly."

Professor Young's paper proposes a new set of rules for the use of carbon border adjustment mechanisms including:

- 1) Limitation of the use of trade mechanisms to truly global environmental problems like climate change and plastics contamination in the world's oceans;
- 2) Mechanism exemptions for imports from any country that has been making an equivalent contribution to the reduction of the environmental problem;

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- 3) A requirement that the import charges take full account of equivalent price signals including indirect signals like Australia's requirement for a proportion of all electricity to be produced from a renewable source;
- 4) Objectivity in the provision of concessions to least developed countries; and
- 5) A requirement that imports from no country be exempted from the mechanism unless in accordance with the proposed principles.

The University of Adelaide's Professor Peter Draper, Executive Director, Institute for International Trade, said: "It is critical that the EU's proposal is consistent with World Trade Organisation rules and does not enable one country to prevent policy choice in another, especially when it can be shown that other policy choices may be equally effective.

"There is a real risk that CBAM could be used as a backdoor way to protect struggling industries from international competition rather than tackling climate change by reducing imports from countries that are seen to be not tackling carbon emissions."

The paper, which was produced with the support of a grant from the Erasmus + Programme of the European Union, may be downloaded from <https://iit.adelaide.edu.au/research/working-papers>

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