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Trade Law And Climate Change: Convergence Or Conflict?

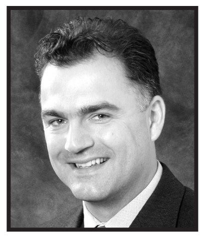
Bernd G. Janzen

AKIN GUMP STRAUSS HAUER & FELD LLP

Last December's United Nations Climate Change Conference in Bali, Indonesia, injected fresh enthusiasm into global efforts to reduce industrial emissions of greenhouse gases blamed for causing climate change. All the major U.S. presidential candidates argue that the United States should adopt a national scheme to sharply reduce greenhouse gas emissions. They also agree that the United States should participate in the global "Bali Roadmap" process intended to work out a successor to the Kyoto Protocol, whose commitments expire in 2012. But national lawmakers and policy-makers entrusted with working out the details face a tricky question: how to compel domestic industries to reduce greenhouse gas emissions when competing industries abroad may be subjected to less stringent emissions requirements – or none at all.

Part of the answer appears to be trade regulation, which is emerging as a mechanism of choice to address such competitive concerns and as a lever to attempt to reduce greenhouse gas emissions in a globally coordinated fashion. However, it is far from clear if the ambitious trade mechanisms under consideration comply or conflict with current trading rules. This article surveys some of the main areas where climate change and international trade regulation are converging or, in some cases, colliding – with significant implications for a wide range of industries that move goods across borders.

Bernd G. Janzen is Counsel in the international trade practice of Akin Gump Strauss Hauer & Feld LLP in Washington, D.C.



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Domestic Legislation – Regulating Imports To Ensure Fair Competition

Of the various recent legislative proposals that would reduce U.S. emissions of greenhouse gasses, the most prominent is the America's Climate Security Act of 2007 ("ACSA"), S. 2191, introduced by Senators Joe Lieberman (D-CT) and John Warner (R-VA) in October 2007. ACSA would establish a national emissions cap on six greenhouse gases, including CO_2, over the period 2012 through 2050, and would institute mechanisms for the allocation of emissions allowances to a range of covered U.S. greenhouse gas-emitting industries. Recognizing the adverse competitive effects that could result to U.S. manufacturing industries competing against foreign industries not subject to such measures – often referred to as the "carbon leakage" problem – ACSA would also require the administration to urge other countries to adopt comparable measures to reduce greenhouse gas emissions.

But also recognizing that a globally coordinated approach to reducing greenhouse gases may not occur, ACSA would, as of 2020, require importers of greenhouse gas-intensive products to declare to U.S. Customs and Border Protection either that (1) the imported goods are covered by special international allowances created under ACSA, or (2) the exporting country is one deemed under ACSA to have taken measures to reduce greenhouse gases comparable to those taken by the United States. The import provisions expressly cover greenhouse gas-intensive manufactured goods such as steel, cement, glass and paper, and would extend to any products that generate, in the course of manufacture, greenhouse gas emissions "comparable" to the expressly covered products. Thus, ACSA has the obvious potential to impose very substantial compliance costs on U.S. importers of a wide range of manufactured goods, and seems certain to alter the competitive balance between U.S. and foreign firms supplying the covered products to the U.S. market.

The trade provisions of ACSA raise the question of U.S. compliance with obligations under the World Trade Organization ("WTO"). The debate centers around the interpretation of Article XX of the General Agreement on Tariffs and Trade ("GATT"), which allows WTO members to take discriminatory action against imports where "necessary to protect human, animal or plant life or health" – but only where such action does not constitute "arbitrary or unjustifiable discrimination" or represent a disguised trade restriction. This is as close as the WTO Agreements come to permitting trade restrictions based on climate change mitigation. Accordingly, U.S. lawmakers are carefully watching the development of WTO jurisprudence on GATT Article XX.

In the most recent case, involving a Brazilian ban on imports of retreaded tires, the WTO Appellate Body found that, while Brazil's import ban by itself constituted a permissible means of protecting human health, the fact that Brazil also permitted imports of retreaded tires from neighboring

AKIN GUMP STRAUSS HAUER & FELD LLP

Please e-mail the author at bjanzen@akingump.com with questions about this article.

MERCOSUR countries resulted in trade discrimination that was not rationally connected to the human health objective of the import ban. Because of this absence of a rational connection between the objective of the import ban and the manner in which it was applied, the import ban did not satisfy the narrow GATT Article XX test. This most recent WTO decision – in particular the rational connection test applied by the Appellate Body – provides an important roadmap for U.S. lawmakers crafting climate change legislation, but by no means answers whether ACSA or other such legislation, once implemented, would pass the GATT Article XX test. The answer matters, because a loss at the WTO could mean that U.S. trading partners receive substantial retaliation rights.

The European Union ("EU") is also contemplating unilateral trade measures that could restrict imports as part of its ambitious drive to reduce carbon emissions across a wide range of industries by 20 percent by 2020. EU leaders such as French President Nicolas Sarkozy and European Commission President Jose Manuel Barroso have repeatedly referred to the possibility of imposing a carbon tax or allowance requirement (similar to the measure contemplated by ACSA) on imports from countries that are not in compliance with Kyoto Protocol emission reduction requirements. These suggestions have drawn strong criticism from U.S. trade officials, who warn that these proposals could facilitate WTO-inconsistent trade protectionism under the guise of environmental protection.

World Trade Organization – Green Trade And Environmental Exceptions

The WTO is grappling with the intersection of trade law and climate change on several fronts. One is the ongoing negotiations toward an Agreement on Trade in Environmental Goods and Services. The mandate for these negotiations, set out in the 2001 WTO Doha Declaration, is the "reduction or, as appropriate, elimination of tariff and non-tariff barriers to environmental goods and services." When originally conceived, this mandate did not expressly include climate change. Nor did it provide any guidance on what goods and services should be deemed "environmental." But the United States and many other WTO members now view a multilateral Agreement on Trade in Environmental Goods and Services as an important tool in combating climate change, and state that this effort complements the process under the United Nations Framework Convention on Climate Change ("UNFCCC").

The basic principle animating the WTO Environmental Goods and Services talks is that trade liberalization for environmental goods and services – e.g., wind turbines and the engineering services required to install and maintain them – will accelerate progress towards common goals such as climate change mitigation. This sector-specific approach to opening foreign markets could present significant opportunities for U.S. businesses exporting environmental technologies to markets such as India, where import duties remain far above the global average.

However, a major rift recently opened up in these talks that brings into doubt any successful conclusion in the near future. Not surprisingly, the debate centers on which goods and services should be considered "environmental." Since late 2007, Brazil has been advocating strenuously for the inclusion of biofuels in the negotiations. According to Brazil, the inclusion of biofuels would ensure that developing countries can increase exports of a good in which they have a comparative advantage, and would advance another chief goal of the Doha Round – that trade liberalization serve the development process. The United States and the European Union have balked at this proposal, instead urging in a joint proposal of December 2007 that the talks be divided into phases, with priority given to trade liberalization for a specified range of technologies related to climate change mitigation and clean energy (not including biofuel). As of this writing, the talks are at an impasse over this issue.

Trends And Observations

Several trends can be discerned as trade and climate change law converge and collide, as discussed above. One is that the political will to sharply reduce greenhouse gases – at least in the United States and the EU – is strong and intensifying. The major U.S. presidential candidates all support the implementation of a national cap-and-trade system to reduce greenhouse gases, and all support U.S. participation in the UNFCCC process. In this political environment, trade law seems to be secondary – i.e., it is useful as a tool to promote climate change mitigation in a manner that ensures that the costs of compliance are shared by domestic and foreign industries. But if U.S. unilateral measures to curb greenhouse gases are found to conflict with WTO trade rules or spur trade retaliation from major U.S. trading partners, the current political environment also suggests that this would be seen as a tolerable cost of addressing what Sen. Baucus has called "the moral imperative to deal with climate change."

The trade-and-climate-change debate is also expanding the notion of what constitutes "unfair" trade. For decades, international trade law, as reflected in both the WTO system and the domestic law of most trading nations, has recognized that pricing imports below certain levels (whether due to "dumping" by foreign exporters or subsidies provided by foreign governments) is a form of "unfair" trade that should be redressed where it harms domestic industries. This notion of unfair trade is based purely on how an imported product is priced. Climate change concerns are now expanding the notion of unfair trade to take into account how imported products are made – specifically, the volume and nature of the greenhouse gases associated with their manufacture. Legislative proposals like ACSA would, in essence, dictate that the price of U.S. imports reflect the externalized environmental costs of greenhouse gas emissions. Just as U.S. antidumping law provides a remedy to domestic manufacturers that must compete against unfairly low-priced, or "dumped," imports, ACSA would provide a remedy to domestic manufacturers that must compete against imports that were manufactured under less stringent greenhouse gas emissions standards – in other words, a remedy against environmental dumping.

Finally, the climate change and trade debate pits multilateralism against unilateralism. The UNFCCC process – the current aim of which is to flesh out the Bali Roadmap with specific goals for a post-Kyoto Protocol agreement – embodies a globally coordinated approach to share the burdens on industry associated with reductions in greenhouse gas emissions. However, the modalities of the burden-sharing have yet to be determined, and it remains unclear how much of the burden developing countries will accept. The less they do, the greater will be the pressure on U.S. and EU lawmakers to ensure, through unilateral trade measures, that their industries are protected from imports produced under less vigorous emissions standards. Political realism suggests that trade mechanisms will be tools of choice in this effort – whether or not they comply with current trade rules.