

## Putting climate change at the heart of trade policy

June 2020

### Summary

If the UK government is serious about addressing climate change, this goal needs to be embedded across all areas of policy, including trade. The hosting of COP26 and negotiation of key trade agreements provide the perfect opportunity for the government to raise the bar, putting climate considerations at the centre of trade policy.

Greener UK has established a set of key principles for the UK's approach to free trade agreements (FTAs). This paper attempts to build on that for climate-related issues to demonstrate the value in linking climate and trade policy more closely.

A new approach should include: leading global conversation on climate and trade; putting climate change mitigation at the heart of free trade agreements; strong defence of high climate-related standards; preferential tariffs for low carbon goods; leeway for the introduction of carbon border adjustments; joint efforts to prevent deforestation and address high emitting sectors; and supporting action on investment and fossil fuel subsidies.

### Introduction

The UK faces a pivotal period in both trade and climate terms. New FTAs are being lined up and negotiated with the US, Japan, Australia and New Zealand, while the government is anxious to make a success of COP26 next year and has signalled its intention to embed decarbonisation into recovery from the devastating effects of the coronavirus.

The risks to the climate from poor trade policies are considerable. FTAs can open up domestic markets to cheaper and higher carbon imports and allow overseas interests to challenge domestic legislation. This would undermine efforts to cut UK territorial emissions, allow more emissions as a whole, and damage nascent low carbon industries. There are some potential positives: FTAs can remove tariffs and harmonise standards at the highest possible level to enable cheaper manufacture and purchase of low-carbon products like photovoltaic cells and electric vehicles, promote sustainable agriculture, and have helped address issues like illegal logging. However, these are currently the exceptions rather than the rule and attempts to use trade in more ambitious ways such as carbon-border adjustments will be challenging.

Nonetheless, trade deals are being drawn up and the urgency of the climate crisis requires its integration into all areas of policymaking. Against this backdrop, **we urge the government to show the climate leadership it is promising and use COP26 and any other opportunities, such as the UK's changed status in the World Trade Organization, to showcase a more climate-centred approach to trade and industrial strategy.**

Another reason for the UK taking a leadership role in this area is that greenhouse gas emissions associated with imports are falling much less rapidly than territorial emissions.<sup>1</sup> Although the Climate Change Act only covers territorial emissions, it is important that the UK doesn't simply replace domestic emissions with imported ones, at the detriment of domestic industries, and does everything it can to reduce its wider impact on the climate.

At the same time, early action on climate change has helped deliver a head start in some low carbon markets, particularly offshore wind. FTAs could enable further trade in these goods, bringing economic benefits to the UK and helping other countries reduce their emissions.

## Fundamental considerations

Greener UK has already established key principles for the UK's approach to FTAs. As a minimum, new trade agreements should:

- Maintain and build on our current high environmental standards
- Are compatible with our environmental and climate goals
- Enable us to reduce the UK's global footprint
- Prioritise goods and services that are low carbon and environmentally sustainable
- Are subject to rigorous scrutiny and oversight, with meaningful and ongoing public participation and accessible information
- Are subject to and respond to environmental impact assessments
- Ban involvement of secret courts like Investor-State Dispute Settlement
- Ensure non-compliance with environmental commitments is properly dealt with

## Climate-specific recommendations

The purpose of this paper is to build on the principles relating to climate change, offering more detailed suggestions on how to make the UK's climate ambition central to its trade policy. Below are key issues we believe need to be considered in developing a climate centred approach to FTAs. This approach should be accompanied by a reinvigorated Industrial Strategy, focused around clean growth, to take advantage of opportunities to export low carbon products and services.

Key issues:

1. **Leading global conversation on climate and trade:** As set out above the UK government should take every opportunity to lead the global conversation on trade and climate, including COP26 and its new status in the WTO. It should **actively engage with the WTO on the organisation's proposed statement on trade and environment**, ensuring this is as ambitious as possible and signing if it appears it will have a meaningful impact and be rigorously implemented.

The UK government should look to join the **Agreement on Climate Change, Trade and Sustainability (ACCTS)** being negotiated by Costa Rica, Fiji, Iceland, New Zealand and Norway.<sup>2</sup> This aims to liberalise trade in environmental goods and services, eliminate fossil fuel subsidies and encourage eco-labelling. The UK's involvement would send a strong signal globally.

2. **Status of climate change mitigation within UK free trade agreements:** The government should prioritise negotiations with countries keen to put climate change and implementation of the Paris Agreement at the centre of an FTA. It should **only seek deep trade agreements going beyond quota and tariff arrangements with those that are signatories to the Paris Agreement and want to show international leadership on climate change**. This aims to leverage greater action on climate change than the UK can manage itself and these agreements should still be subject to all the recommendations set out elsewhere in this paper. The UK government would not be alone here: Brazilian deforestation has been a key factor in EU leaders' concerns about the draft EU-Mercosur trade agreement.

To support this, future FTAs should include a review clause that would apply should parties weaken implementation of the Paris Agreement or other climate-related multilateral environmental agreements (MEAs). An independent body would be needed to decide whether this has happened.<sup>3</sup>

Future UK FTAs must be very clear that **MEAs relating to climate change, and their implementation, have supremacy over trade measures should there be a conflict.** This is important because trade agreements are more often used as the basis for legal challenges than MEAs.<sup>4</sup> Commitments to MEAs are common in FTAs but often written in vague or non-binding language and included in easily overlooked sustainable development chapters.

3. **Strong defence of high climate-related standards:** Trade policy often aims to remove non-tariff barriers to trade and trade agreements regularly put in place mechanisms to achieve this such as commitments to regulatory cooperation. However, these efforts often prioritise trade over measures intended to protect public health and the environment and risk slowing the rate at which further protections are introduced. There has also been long-running opposition to legally justifiable measures that distinguish between so-called 'like' products that appear the same but have been produced with different environmental impacts, differentiating them in the eyes of customers and in their fit with importing countries' environmental commitments.

**If the UK aims to be a leader on climate change, it must be clear that it will regulate in the best interests of the climate and be active in promoting this approach via the WTO and its various mechanisms.** This includes the settlement of trade disputes, where there are already efforts to give more consideration to environmental concerns that the UK could help support. It is also worth noting that some types of climate policies flagged by trade lawyers as contentious, such as mandatory ecolabels and bans on unsustainable products, have been in place unchallenged for years for some products.

This approach must not be undermined by investment measures that deter lawmakers from more ambitious policies on the grounds that it could change the investment environment. The risks in this area have been highlighted by some prominent cases, such as that of Vattenfall AB contesting environmental permit conditions for a new coal fired power plant in Germany.<sup>5</sup>

Greener UK is keen to ensure close cooperation with EU as the UK's closest trading partner and largest market, and a trusted partner in past environmental action. For this reason, the FTA with the EU should be treated separately allowing much closer cooperation on trade and non trade-related elements of climate and environmental policy.

However, in other trade negotiations the government should press for mutual respect of each other's high standards, allowing each party to take as rapid action as possible, and to work together to further that ambition, rather than embedding a cooperative approach to regulation.

Finally, commitments by both sides to a meaningful and enforceable non-regression provision must be a basic component of all future FTAs.

4. **Preferential tariffs for low carbon goods:** Global decarbonisation could be achieved more cheaply if more climate friendly goods and services such as photovoltaic panels, energy efficient appliances and sustainably produced foods were tariff free. Reflecting this, there have been multilateral efforts to remove tariffs for green goods under the Environmental Goods Agreement (EGA) but these have stalled. At the same time, moving more rapidly to address climate change than many other major economies has added costs for some UK businesses that their overseas competitors have not faced. **While recognising that tariffs should never be a substitute for strong regulatory approaches, the government should seek opportunities to help build a global system that supports production and deployment of low carbon goods and technologies over existing alternatives.**

There is a balance to be struck. Lowering tariffs on some products would expose emerging domestic low carbon technologies to untenable competition and must be managed carefully, but the principle should be to support trade in low carbon goods. This means the UK government should, in consultation with UK stakeholders and based on regular impact assessment of existing and proposed tariff schedules, aim to reduce tariffs on greener goods wherever possible inside and outside FTAs and seek equivalent arrangements from trading partners.

There are differing definitions of green goods and government should ensure that the UK's definition is ambitious. This should include products like photovoltaic panels that reduce greenhouse gas emissions, products that are more energy or carbon efficient in operation than competitors and products in other categories that have lower than average embedded carbon. However, there must be a robust underlying methodology to ensure individual products are genuinely low carbon and that low tariffs are not used to support the 'least polluting' forms of products where much more sustainable alternatives exist.

This kind of approach must be balanced against support for a just transition in developing countries. Possible solutions here might include refraining from using such clauses for a pre-agreed period and supporting local operators to enable them to meet higher standards.

The UK should also continue to support efforts to reach a deal under the EGA, which the European Commission estimated in 2016 could boost trade flows in green goods by €21bn.<sup>6</sup>

5. **Provide leeway to introduce carbon border adjustments (CBAs):** Building on the points set out above, the government should ensure there is potential to introduce more robust approaches such as CBAs in future. CBAs would help address carbon leakage issues as well the carbon embedded in imported goods and over time may help retain a link to the EU Emissions Trade System (ETS) as the government currently aims to do. A CBA would be introduced unilaterally, not through FTAs or, potentially, tariff schedules, but it is important that these do not narrow future options. Most discussion of CBAs has focused on industrial products and energy supplies but it is important to consider how they could also be applied to reduce the climate and nature impacts of agricultural goods.

6. **Joint effort to prevent deforestation and address high emitting sectors:** The UK should rapidly phase out import of products associated with deforestation. It should also work with future trade partners to identify other sectors or products that make a significant contribution to their carbon footprints and establish a process to cooperate on reductions. This would help the UK target parts of its overseas supply chain that are particular sources of embedded carbon emissions, for instance by encouraging renewable energy generation, and could open the door to technology transfer where appropriate.
  
7. **Fossil fuel subsidies and investments:** The UK should set a positive example in its trade policy by agreeing to a time-bound phase out of tax relief and other financial support for fossil fuels. It should also consider requiring transparency from UK-listed companies about overseas investments in fossil fuel extraction which could undermine trade partners' attempts to decarbonise. It should expect developed country partners to make similar commitments.

It is also essential that provisions on investment, including Investor-State Dispute Settlement and any agreements outside FTAs, are not allowed to undermine countries' climate change policies either directly as in the Vattenfall example or by a more subtle 'regulatory chill' effect on policymakers.

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## Endnotes

<sup>1</sup> Defra, 2020, UK's Carbon Footprint 1997 – 2017

<sup>2</sup> [www.mfat.govt.nz/en/trade/free-trade-agreements/climate/agreement-on-climate-change-trade-and-sustainability-accts-negotiations/](http://www.mfat.govt.nz/en/trade/free-trade-agreements/climate/agreement-on-climate-change-trade-and-sustainability-accts-negotiations/)

<sup>3</sup> TJM and T&E, 2017, Can trade and investment policy support ambitious climate action?

<sup>4</sup> Economist Intelligence Unit, 2019, Climate change and trade agreements: Friend or Foe?

<sup>5</sup> Greener UK, 2019, Priorities for trade and the environment through Brexit

<sup>6</sup> European Commission, 2016, Trade Sustainability Impact Assessment on the Environmental Goods Agreement

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