

The Use of CBAM Revenues

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Current status

- Currently, CBAM Regulation does not specify how revenue from the CBAM will be allocated and spent.
- The current Commission proposal on **the new own resources** with respect to the CBAM revenues envisions a solution whereby a percentage (25%) of the revenues would be retained by EU Member States with the rest accruing to the EU's own resources, to repay the NextGenerationEU pandemic recovery package.

Analytical framework

- i. Delivering CBAM's objectives**
- ii. Alignment with the principle of *Common But Differentiated Responsibilities and Respective Capabilities* (CBDR&RC)**
- iii. International climate finance**
- iv. Legal feasibility under WTO and the international climate regime**
- v. Principle of mirroring the EU ETS**
- vi. Political acceptability of the CBAM in the EU and abroad**
- vii. Order of magnitude and permanence of available funds**

Should revenue be recycled? (1)

- Reasons *for* recycling revenue:
 - **Support CBAM objectives:** Using revenue to invest in industrial decarbonization domestically or abroad helps reduce leakage risk and lower global emissions
 - **Mitigate negative welfare impacts:** Use of revenue can serve to relieve negative impacts on vulnerable trade partners or on affected stakeholders in the EU
 - **Improving alignment with international law:** Use of revenue for industrial decarbonization strengthens the case of CBAM under GATT Art. XX (b) and (g)
Investment in developing countries can help address concerns about the CBAM being misaligned with the CBDR-RC principle and the architecture of the Paris Agreement
 - **Providing a new source of climate finance:** Committing revenue to international climate finance could help reduce the financing gap
 - **Improving diplomatic relations:** Returning revenue to trading partners could forestall or alleviate diplomatic tensions emerging over the CBAM
 - **Matters of principle:** Returning revenue to those who pay mirrors the EU ETS

Should revenue be recycled? (2)

- Reasons *against* recycling revenue:
 - **CBAM cost incidence distinct from payment obligation:** actual cost burden passed through to EU consumers; general budget can be used for compensation measures
 - **Wealth transfers to competitors or geopolitical rivals politically unpopular:** returning large amounts of revenue to e.g. China will not win domestic votes
 - **Competition with traditional climate finance and development assistance:** claiming returned CBAM revenue as climate finance could raise questions about additionality; also potential for duplicating existing ODA structures
 - **Risk of violating WTO rules:** if revenue is allocated to domestic companies, it could be considered a prohibited subsidy; if foreign entities, selection could be discriminatory
 - **Potential to undermine CBAM objectives:** revenue recycled to foreign firms could weaken the incentive to reduce emissions and dilute the carbon cost equalization
 - **Not enough revenue to spur decarbonization:** direct revenue from sale of CBAM certificates would not suffice to meaningfully decarbonize foreign industries anyway

To whom? How much recycled, and through what channels?

- How much recycled, and through which channels?
- The available funds are not all that significant
- Should they be split, and how?
- What conditionalities should guide their disbursement (if earmarked)?
- Through what channels should they be disbursed (if earmarked)?
- Avenues for cooperative funding?

Takaways

1. As a matter of principle, and to have a treatment similar to how revenues are used under the EU ETS, a significant amount of CBAM revenue should be used towards decarbonization of exporters in countries that are most impacted by the CBAM and are least capable of adapting to those impacts.
2. Funding should be ensured for the administrative costs of the EC, not only in the Member States.
3. It is important, possibly essential, for the credibility of the EU and its international diplomacy that the CBAM revenue not be counted towards international climate finance contributions of the EU. This is especially true in light of the efforts being made by the EC to set up new structures for international diplomacy, and the promotion of carbon pricing.
4. CBAM funds should be returned to enterprises and not governments. They could be directed to firm-level decarbonization and awarded by reverse auction, which would retain how the CBAM mirrors the EU ETS and its treatment of domestic enterprises. Similar to free allocation, the allocation of funds could be made conditional upon the development of non-prescriptive commitments (ideally a road map or maybe a commitment) for enterprise decarbonization, and the funds should be used for very specific projects, rather than a general refund. Alternatively, they could be directed to softening the impacts of compliance for exporters, for example subsidizing the verification of GHG-intensity data.
5. One alternative that should be considered is the creation of a fund that could disburse the CBAM revenue, but that means that a certain critical amount needs to be collected in order to make this fund impactful and economically efficient. That may be achieved by potentially pooling funds from a number of countries that have their own border carbon adjustment (BCA) measures, which could lead to the formation of a very simple “Carbon Club” to disburse money potentially through a reverse auctioning approach – to exporting enterprises that meet certain criteria in certain countries.