	REPUBLIC OF TURKEY **MINISTRY OF TRADE** **6 April 2020**

VIEWS OF THE GOVERNMENT OF TURKEY ON THE CARBON BORDER ADJUSTMENT MECHANISM WITHIN THE FRAMEWORK OF THE INCEPTION IMPACT ASSESSMENT

1. General Remarks

The European Green Deal adopted by the European Commission (hereinafter referred as "the Commission") on 11 December 2019 includes the goal of enshrining the long-term objective of climate neutrality by 2050 in legislation and increasing the EU's climate ambition to reduce greenhouse gases emissions by 50-55% from 1990 levels by 2030. The European Green Deal also indicates carbon leakage risk, which occurs when production is transferred from the EU to other countries with lower ambition for emission reduction, or when EU products are replaced by more carbon-intensive imports.

In this vein, the Commission initiated the "Inception Impact Assessment for Carbon Border Adjustment Mechanism" on 4 March 2020. The initiative indicates that in terms of the type of the policy instrument various options could include a carbon tax on selected products – both on imported and domestic products, a new carbon customs duty or tax on imports, or the extension of the EU ETS to imports.

Turkey welcomes the increased ambition and efforts of the EU to tackling climate and environmental-related challenges announced by the European Green Deal. However, Turkey also believes that EU's transition to a green economy should not result in protectionist measures, but should focus on building partnerships that would contribute to EU's strategic vision.

The effects of the measure on the EU, as well as on the significant suppliers of the EU have to be thoroughly analyzed. Turkey and the EU are linked by a Customs Union partnership (CU Decision), and trade in coal and steel products are governed by the Turkey-ECSC Free Trade

Agreement (FTA) and trade in agricultural products by Decision No. 1/98. Turkey’s exports volume to EU was about 88 billion dollars in 2019 and EU’s share in total Turkey’s exports is about 49%. There are a number of EU companies operating in Turkey, and companies that are part of European value chains. Before the implementation of any measure, EU should carefully examine the effects of any measure on bilateral trade and on value chains.

Moreover, EU should ensure compatibility with the aforementioned bilateral arrangements, as well as with World Trade Organization (WTO) rules and the international obligations of the EU especially arising from United Nations Framework Convention on Climate Change (UNFCCC), and hold necessary consultations with Turkey in line with EU’s international obligations. In that regard, Turkey would like to recall the Commission’s obligation to consult Turkey on the same basis as Member States, in areas of directly relevance to the proper functioning of the Customs Union (CU) in line with Article 59 of Decision No. 1/95.

Enabling a just and inclusive transition of all industries throughout the whole value chain is critical. In that respect, financing is inevitably at the heart of the transition to achieve the objectives of the Green Deal. The fact that the EU positions itself as a global leader requires the EU to be at the forefront of coordinating the international efforts towards a sustainable and inclusive financial system as well as to mobilize its own financial resources for its partners to join the EU on a sustainable path.

Turkey hereby would like to submit its views, and the issues for which further clarification is requested, regarding the inception impact assessment on the carbon border adjustments initiated by the Commission.

A. TURKEY’S VIEWS REGARDING THE INCEPTION IMPACT ASSESSMENT ON CARBON BORDER ADJUSTMENTS

Turkey would like to note that carbon border adjustments proposed by the EU should comply with the provisions of the CU Decision, the FTA on coal and steel products between Turkey and the EU, and Decision No. 1/98 on agricultural products. Any carbon border adjustment mechanism should also be in conformity with the rules of WTO and the international obligations of the EU; especially arising from UNFCCC.

Along with these international obligations that the EU must comply with in the implementation of a carbon border adjustment mechanism, Turkey also would like to present its remarks on the methodology proposed by the EU as well as the financing aspect of the carbon border adjustments which lies at the heart of this mechanism.

1. Remarks on Carbon Border Adjustments within the Framework of Bilateral Obligations between Turkey and the EU

In line with the objectives set out in the Ankara Agreement and the Additional Protocol, Turkey and the EU established a CU in 31 December 1995. In addition, for products covered by the European Coal and Steel Community (ECSC), the Parties complemented the CU with the Turkey-ECSC FTA signed on 25 July 1996 and for agricultural products with Association Council Decision No.1/98 of 25 February 1998.

Article 4, 5 and 6 of the CU Decision explicitly rules that import or export customs duties and quantitative restrictions on imports and exports and other charges or measures having equivalent effect shall be prohibited between the parties.

Although the CU Decision allows for exceptions to the provisions of Articles 5 and 6 (the elimination of quantitative restrictions or measures having equivalent effect) under Article 7, **it does not allow any exception to Article 4 on the elimination of customs duties and charges having equivalent effect. Additionally, Article 4 clearly stipulates that the Community and Turkey shall refrain from introducing any new customs duties on imports or exports or any charges having equivalent effect from the date of entry into force of the CU Decision.**

Moreover, the grounds under which the Parties are allowed to stray from Article 5 and 6 of the CU Decision are specifically determined under Article 7, where it is also envisaged that any measures on the grounds stipulated in Article 7 shall not constitute a means of arbitrary discrimination or a disguised restriction on trade between the Parties.

In this regard, we would like to underline that the introduction of **any new customs duty or tax on imports is clearly forbidden in Decision No. 1/95. Moreover, quantitative restrictions or measures having equivalent effect which constitute a means of arbitrary discrimination or a disguised restriction on trade between the Parties would also be in contradiction with the CU Decision. Turkey would like to note that any policy instrument that would be applied in contradiction with the Articles 4 and 7 of the CU Decision would impair the free movement of goods between the Parties.**

On the other hand, **the FTA on coal and steel products between Turkey and EU also prohibited introducing customs duties, quantitative restrictions and charges and measures having equivalent effect in trade of these products between Turkey and the EU (Article 3 and 4)**. The FTA allows for the Parties to take appropriate measures, only within the framework of countervailing measures (Article 7.6), anti-dumping procedures (Article 10), safeguard measures (Article 12) and practices incompatible with Article 3 and 4 (Article 5) under the conditions specified in the FTA. **Considering that carbon border adjustments of the EU does not relate to any of these grounds of exception to the free trade between the parties, the introduction of a customs duty, quantitative restriction, or charges and measures having equivalent effect would be incompatible with Article 3 and 4, and the proper functioning of the FTA between the parties.**

Similarly, **Decision No. 1/98 determines the preferential regime to be applied between the Parties, and also prohibits quantitative restrictions on imports and exports of agricultural products and all equivalent measures. Any measure on imports taken by the EU would be in contradiction with the relevant Decision, as well.**

In addition, **Turkey would like to recall the Commission’s obligations stemming from the consultation and decision-making provisions of Decision No. 1/95**. In that respect, since the EU is considering the introduction of a customs duty, tax on imports or the extension of EU ETS to imports, Turkey is expecting the Commission:

- **to consult Turkey on the same basis as Member States** in line with Article 59 of Decision No. 1/95;

- **to cooperate with Turkey in good faith** during the information and consultation phase with a view to **facilitating, at the end of the process, the decision most appropriate for the proper functioning of the Customs Union.**

2. Remarks on Carbon Border Adjustments Within the Framework of UNFCCC

2.a. Remarks on Carbon Border Adjustments and Common but Differentiated Responsibilities Principle

The European Green Deal emphasized that "*should differences in levels of ambition worldwide persist, as the EU increases its climate ambition, the Commission will propose a carbon border adjustment mechanism, for selected sectors, to reduce the risk of carbon leakage*". Alongside with carbon leakage risks, there is also urgency of climate change action by international community taking into account Paris Agreement's aim for holding the increase in the global average temperature to well below 2°C above pre-industrial levels and pursuing efforts to limit the temperature increase to 1.5°C above pre-industrial levels. Therefore, combating climate change at international community plays a vital role and all members of international community should take necessary steps to combat climate change.

However, **as countries have different social and economic conditions and capabilities, UNFCCC adopts the principle of "common but differentiated responsibilities"** and stipulates that "*The Parties should protect the climate system for the benefit of present and future generations of humankind, on the basis of equity and in accordance with their common but differentiated responsibilities and respective capabilities*." (Article 1). Common but Differentiated Responsibilities and Respective Capabilities is a principle within the UNFCCC that acknowledges the different capabilities and differing responsibilities of individual countries in addressing climate change. In this vein, Article 2.2. of Paris Agreement stipulates that "*This Agreement will be implemented to reflect equity and the principle of common but differentiated responsibilities and respective capabilities, in the light of different national circumstances*."

In line with common but differentiated responsibilities and respective capabilities, in the system of Paris Agreement, Parties decide on their mitigation and adaptation measures and the level of ambition in accordance with their own capabilities and conditions. Article 4.2 of Paris Agreement also stipulates that "*Each Party shall prepare, communicate and maintain successive nationally determined contributions that it intends to achieve*." Turkey also presented its own Intended Nationally Determined Contribution (INDC) towards achieving the ultimate objective of the UNFCCC which is set out in its Article 2 and clarifying information in accordance with its own conditions and capabilities.

In the light of basic rules and principles of international climate change regime, differences in levels of ambition worldwide are inevitable and acceptable as countries have different level of conditions and capabilities. Therefore, Turkey is of the view that carbon border adjustments for imports would be incompatible with these rules and principles.

2.b. Remarks on Carbon border Adjustments as Trade Restrictions

As Article 3.5 of UNFCCC stipulates that "*The Parties should cooperate to promote a supportive and open international economic system that would lead to sustainable economic growth and development in all Parties, particularly developing country Parties, thus enabling them better to address the problems of climate change.* ***Measures taken to combat climate change, including unilateral ones, should not constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade***", measures addressing climate change should be compatible with sustainable economic growth and development goals and should not be a disguised restriction on international trade.

Therefore, Turkey has concerns that unilateral actions like carbon border adjustments risk creating trade barriers and could be used as a protectionist tool in international trade which could lead to trade retaliations, risk becoming a stumbling block in the international climate change negotiations and consequently give harm to both rule-based international trade and international climate change negotiations. It would be more appropriate to avoid using unilateral actions and resort to other methods to diminish effects of carbon leakage. On the other hand, if a carbon border adjustment measure is to be applied, it should be done in a manner to least disturb trade, should not be designed as a disguised restriction and should take into account the principles of UNFCCC such as equity and common but differentiated responsibilities.

2.c. Remarks on Carbon Border Adjustments and Response Measures

The UNFCCC affirms that responses to climate change should be coordinated with social and economic development in an integrated manner with a view to avoiding adverse impacts on the latter, taking into full account the legitimate priority needs of developing countries for the achievement of sustained economic growth and the eradication of poverty and Article 10 of UNFCCC stipulates that "*The Parties shall, in accordance with Article 10, take into consideration in the implementation of the commitments of the Convention the situation of Parties, particularly developing country Parties, with economies that are vulnerable to the adverse effects of the implementation of measures to respond to climate change. This applies notably to Parties with economies that are highly dependent on income generated from the production, processing and export, and/or consumption of fossil fuels and associated energy-intensive products and/or the use of fossil fuels for which such Parties have serious difficulties in switching to alternatives*."

In this regard, international climate change regime takes into account that mitigation measures can affect social and economic development of countries. Members of international community should not ignore negative impacts of implementations of response measures.

Turkey's exports volume to EU is about 88 billion dollars in 2019 and EU's share in total Turkey's exports is about 49%. Taking into account the EU's share in Turkish exports, any kind of climate related trade measure would affect Turkey's exports, economy and development needs and goals. In this respect, **Turkey requests EU to take into account the possible negative effects of a carbon border adjustment mechanism on Turkey and other exporting countries. It would be appropriate to discuss social and economic effects of this kind of carbon border adjustment under UNFCCC negotiations.**

3. Remarks on Carbon Border Adjustments Within the Framework of WTO Rules

The document contains information that the adjustment will be designed by taking into account the carbon content of the product. It is stated that "a carbon border adjustment mechanism would ensure that the price of imports reflect more accurately their carbon content". Besides, it is stated that the regulation will be carried out in accordance with the WTO rules. Although, more detailed information is needed on how the EU will design this regulation accordingly, Turkey would like to note some considerations needed to be taken into account under WTO/GATT rules in the design of a carbon border adjustment.

First of all, a carbon border adjustment whether it takes the form of a new carbon customs duty or tax on imports or a carbon tax both on selected imported and domestic products requires that it is imposed on **"like" products of all WTO contracting countries and does not exceed the equivalent domestic tax.** Articles I (MFN), II and III (National Treatment) of the GATT permit a measure only under these conditions.

However, within the framework of the WTO law and precedent, there are no criteria used regarding the "carbon content" of a product in defining a "like" product. Per the WTO Appellate Body, "likeness" is, "fundamentally, a determination about the nature and extent of a competitive relationship between products." There are four pertinent criteria: "(1) the properties, nature, and quality of the products; (2) the end uses of the product; (3) consumers' tastes and habits; and (4) international tariff classification". These criteria greatly complicate the case for differentiating for instance between a car which is manufactured using renewable energy and fossil fuels as the manufacturing process will not change the final product.

Even in the hypothetical case that the carbon content is accepted as a new criterion in the determination of "likeness", this would require some means to determine the carbon content of imported goods and to assess the tax appropriately to that content. In this regard, the carbon border adjustment must consider imports of covered goods for which information is not available or is too difficult to collect. In particular, **it must not violate the WTO TBT Agreement, which protects developing nations that may not have adequately integrated the measurement and reporting standards necessary to comply.**

Besides, **in accordance with Article II and III of GATT, any carbon customs duty or internal tax on imports that is planned to be applied as a carbon border adjustment**

mechanism should be compatible with the national treatment rule, thus has an impact of equal burden with that of the domestic producers. In this context, considering that the ETS is the major policy tool in regulating carbon emissions in the EU, transparent explanations are needed on how the burden the ETS brings to domestic products will be converted into an equivalent charge or tax on imports. In addition, **free allowances to EU sectors, the gains obtained from the sale of allowances by EU firms, compensations and ETS funds reallocated to the green transformation of EU firms have also to be taken into account in considering the burden placed on domestic products.**

Regarding with the other policy option, namely extension of the EU ETS to imports can be considered as a quota and classified as a quantitative restriction in accordance with GATT Article XI. Therefore, it will be essential for the EU to elaborate on how this policy option will be planned to comply with the WTO rules and obligations of the EU.

Moreover, Turkey is of the opinion that a carbon border adjustment also risks being considered as "**an arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade" under GATT Article XX**. Turkey has some concerns that the methodology indicated for the carbon border adjustments would cause discrimination against imports and a disguised restriction on international trade violating the fundamental principles embodied in the chapeau of GATT XX. Please find Turkey's detailed remarks on the methodology of the carbon border adjustments in paragraph 4 below.

In the light of all this information, **the parameters of the measure to be implemented by the EU should be put forward in a transparent and detailed manner** in order to prepare the trade partners. In any case, the **EU, as it has been already stated, has to ensure any measure to be compatible with the WTO rules.**

4. Remarks on the Methodology of Carbon Border Adjustment

According to the methodological approach to evaluating the carbon content and carbon pricing of imported products proposed by the Commission, it is stated that a carbon border adjustment could be based on similar methodological considerations as for EU ETS, i.e. benchmark values, unless the exporter certifies a lower carbon content and/or a higher carbon cost at origin. It is also indicated that the Commission will also look at alternative approaches, e.g. defining carbon content of products, taking into account their interaction with existing and future climate policies.

The methodology requires "the same benchmark values" applied to all exporting countries or "defining the carbon content of the products" without any **special approach according the specific conditions and economic development levels of countries.** Moreover, it is unclear whether the methodology is able to recognize and adjust when other national policies, good practices or regulations beyond domestic carbon prices and taxes have led to reduced GHG emissions and benefits to the environment. Turkey is of the opinion that the methodology should include a fair, transparent and predictable process in the application of border carbon adjustment, which **does not:**

- inevitably result in **discriminatory and arbitrary application against imports and a disguised restriction on international trade** in violation with EU's bilateral obligations, the GATT XX and the principles of UNFCCC,

- **hamper the green transition of the industries of developing countries** by negatively affecting their export capacities via increasing the cost of imports from these countries,

- **create a complex and unfair administrative burden on the exporters** of the developing countries, especially on the SME exporters which would also damage their green transformation efforts

Furthermore, **countries' measures and efforts for pricing carbon emissions implicitly and for decreasing emissions of electricity production (through investments in renewable energy), as well as other national policies, good practices or regulations and other taxes beyond domestic carbon prices and taxes that have led to reduced GHG emissions and benefited the environment should also be considered throughout the design of such an adjustment mechanism.**

Hence, **it would be important to involve the affected country and also allow foreign producers to prove that the carbon intensity of their products is lower than a benchmark set by the EU** (border carbon adjustment implementing country). However, such possibilities should not result in complex and unfair administrative burden on the exporters, and especially SMEs in a way that would negatively affect their export capacities and curtail their competitiveness in the international trade.

Moreover, another way of strengthening the fairness of the border carbon adjustment is to afford foreign producers **necessary time to increase their domestic climate policy efforts.** Additionally, EU Commission must engage in **serious, across-the board consultations with countries with bilateral agreements** before imposing the border carbon adjustment. This requires serious good faith efforts to reach an agreement on the part of EU.

Other requirement related to the discrimination against countries where the same conditions prevail is that border carbon adjustment measure must be applied with **"sufficient flexibility" to take into account the specific conditions and levels of economic developments of countries** (Turkey) in line with the principle of **common but differentiated responsibilities and respective capabilities** applied in UNFCCC.

5. Remarks on the Financing Aspect of Carbon Border Adjustment

As correctly mentioned in the Green Deal, delivering additional reductions in emissions is a challenge which requires massive public investment and increased efforts to direct private capital towards climate and environmental action, while avoiding lock-in into unsustainable practices.

In this regard, the Commission has recently presented a Sustainable Europe Investment Plan to help meet the additional funding needs for the transition and transition of its sectors. It combines financing from different sources such as the EU Budget, the InvestEU Fund, the Just Transition Mechanism and State aid guidelines to support green investments. The Green Deal also says that the Commission will support clean steel breakthrough technologies leading to a zero-carbon steel making process by 2030 and will explore whether part of the funding being liquidated under the European Coal and Steel Community can be used. In addition, the auction revenues by the member states is also used for domestic and EU climate and energy purposes. The split between revenues used for domestic and EU purposes compared to revenues used for international climate finance is about 90%/10%.[1]

There is no doubt that the EU is largely subsidizing the green transformation through the use of a number of instruments. However, **not all the trading partners of the EU possess equivalent financial means or have the same capacity to respond.**

In line with above-mentioned considerations Turkey welcomes that the EU states in the Green Deal that

"…The environmental ambition of the Green Deal will not be achieved by Europe acting alone. The drivers of climate change and biodiversity loss are global and are not limited by national borders. The EU can use its influence, expertise and financial resources to mobilise its neighbours and partners to join it on a sustainable path. The EU will continue to lead international efforts and wants to build alliances with the likeminded…"

In this regard, it is clear that there is a huge funding gap between Turkey and the EU to respond the climate change and hence access to **adequate funding would be key for supporting green transformation** in Turkey and companies established in Turkey, including EU companies and companies participating to EU value chains. To that end, any measure that may be introduced between Turkey and EU without the introduction of adequate and equal financing opportunities would significantly harm the level playing field between Turkish and European operators. Hence, **consultations on the subject matter need to take into account the financing aspect of green investments and should aim to provide Turkey access to the European Green Deal Investment Fund, and other funds available for green transformation.**

Another important issue regarding the financing aspect that should be taken into account is related to the revenues to be collected by Europe via the carbon border adjustments on imported products. Those revenues should be transferred back to the concerned countries for their own climate and energy investments instead of being used for further subsidizing investment in the EU.

[1] Analysis of the use of Auction Revenues by the Member States; Final Report; EU Commission; March 2017.

B. REMARKS ON ISSUES THAT NEEDS CLARIFICATION BY THE COMMISSION

1. Remarks on Carbon Border Adjustments on Imports and Exports

A carbon border adjustment scheme can be applied to imports, exports or both. However, the impact assessment document on the carbon border adjustment does not indicate carbon border adjustments on EU's exports and stipulates that "*A carbon border adjustment measure would apply to imports into the EU.*" Turkey would like EU to clarify its position on carbon border adjustments on exports.

As the impact assessment document refers to border adjustment measures only for imports, it should be noted that Turkey's views on this paper are focused on carbon border adjustment measures for imports.

2. Remarks on Scope of Carbon border Adjustment

The impact assessment document indicates that various options for a carbon border adjustment could include a carbon tax on selected products – both on imported and domestic products, a new carbon customs duty or tax on imports, or the extension of the EU ETS to imports. However, the scope of possible carbon border adjustment is not clear yet in terms of sector and exporting country. Turkey would like EU to clarify about whether carbon border adjustment mechanism would apply to imports from all countries and there would be differentiation in terms of exporting country.

In any case, Turkey would like to note that a **gradual application in terms of the sectoral scope** of the carbon adjustment is required that would afford third countries necessary time to increase their domestic climate policy efforts. It is also critical that a **sufficient period of transition is recognized to allow sectors and companies**, especially SMEs to adapt themselves to the changed circumstances and possible new requirements stemming from a carbon border measure.

C. CONCLUSION

In line with above considerations, Turkey would like to express its concerns regarding any border carbon adjustment mechanism by the EU since unilateral actions like carbon border adjustments on international trade **risk creating trade barriers and being used as a protectionist tool which could lead to trade retaliations** notably in times of trade wars and unilateral impositions of additional tariffs.

Turkey has serious **concerns on the compatibility of such a measure with Turkey-EU Customs Union and other bilateral arrangements, as well as WTO rules and principles of UNFCCC**. Hence, this could give harm to both Turkey-EU bilateral trade and the rule-based international trade order, as well as international climate change negotiations.

In that regard, Turkey believes that it would be more appropriate to avoid using unilateral actions and to resort to other methods to diminish the effects of carbon leakage. Instead, Turkey believes that the EU's efforts to tackle climate change should focus on building partnerships that would contribute to EU's strategic vision and support the efforts of companies in Turkey in that respect.

However, if a carbon border adjustment measure is to be applied, in its design Turkey hereby requests:

- the provisions of CU Decision, Turkey-ECSC FTA and Decision No. 1/98 to be fully taken into account,

- the different capabilities and differing responsibilities of EU's trading partners in addressing climate change as well as the possible negative effects of carbon border adjustments on Turkey and other exporting countries on the achievement of sustained economic growth be taken into consideration in line with the principles of UNFCCC,

- carbon border adjustment mechanism to be applied in a manner that least disturb trade and does not constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade in line with the rules and principles of UNFCCC and WTO,

- application of a fair, transparent and predictable methodological approach in the application of border carbon adjustment which includes some flexibilities and/or a special approach according the specific conditions and economic development levels of countries, notably of the developing countries;

- consideration of other national policies, good practices or regulations and other taxes beyond domestic carbon prices and taxes that have led to reduced GHG emissions and benefits to the environment,

- provision of an inclusive finance mechanism and improvement of cooperation opportunities with the EU to enable the mobilization of both EU and international funds.

Finally, Turkey is closely monitoring the legislative process of the carbon border adjustment mechanism and reserves all its rights stemming from our bilateral agreements, WTO Agreements, UNFCCC and other relevant international agreements.