In December, the EU provisionally adopted a carbon tariff on imports. The official name is the Carbon Border Adjustment Mechanism, or CBAM for short. The purpose of the mechanism is that EU companies, unlike many in other countries, have to pay a price for the carbon emitted in manufacturing. They need a border adjustment to remain competitive. As the chair of the EU environment committee put it: "The message to our industries is clear: there is no need to relocate because we have taken the necessary measures to avoid unfair competition and carbon leakage."

Lord Stern, the eminent climate economist, has argued for narrowly focused CBAM's:

> "CBAMs have to be intelligent. They have to be simple in definition and in operation and focused on a narrow group of relevant industries such as steel and cement. If you explain to other countries what you have in mind, and that they will not be affected if they have the right policies, then you can have a constructive dialogue. But if you use them as blanket protectionism, that would be divisive. And it is important to recognize that other countries may pursue sustainable growth and emissions reductions in different ways, and you should not insist that every country uses a carbon price, notwithstanding the great value of that policy tool."

In line with this observation the current version of CBAM would cover five industries: cement, aluminum, fertilizers, electric energy production, iron and steel.

In the initial phase, importers would only be required to file information reports on the carbon emissions connect with their goods. Meanwhile, grants of free carbon allowances to the relevant industries will be phased out. After that transition period, EU importers must purchase CBAM certificates covering the emissions associated with the products they import and submit annual CBAM declarations.

There is no exact precedent in world trade law for these border adjustments. Trade experts generally seem to believe that the border adjustments would not violate WTO requirements if they only offset the price on carbon paid by domestic industry.

The U.S. has also proposed a multilateral adjustment mechanism for the steel industry. According to the NY Times:

> "The proposed group, known as the Global Arrangement on Sustainable Steel and Aluminum, would wield the power of American and European markets to try to bolster domestic industries in a way that also mitigated climate change. To do so, member countries would jointly impose a series of tariffs against metals produced in

> environmentally harmful ways.”

The threat of these border adjustments is one reason that investors worry about a company’s carbon emissions. They’re also why many major investors support the SEC’s proposed carbon disclosure rules, so the investors can get the information they need to forecast industry costs.

As the CBAM illustrates, we are past the time when each country could decide in isolation on its climate policy. The EU’s actions are an early sign of the economic pressures that will increasingly be brought to bear on countries with laggard industries. Carbon border adjustments have been talked about for a long time. Now they are about to get real.