Introduction

Taxation is a powerful policy instrument. Though the primary purpose of taxes is to raise revenue, taxation often reflects policy choices. Moreover, taxes sometimes serve as a direct tool for pursuing non-budgetary objectives. A good example of this is environmental taxes.

Taxation is a powerful policy instrument not only at the domestic level, but also at the international level. The phenomenon of harmful tax competition highlights how one state’s decision to design harmful tax policies (for example, by lowering tax rates or refusing to exchange information) may have an impact on other states. Bilateral tax agreements through which two states agree as to the allocation of taxing rights on cross-border income also illustrate the role of taxation in international relations. A third example concerns border taxation on ‘internationally traded goods’, such as taxes on imported products. To a certain extent, each of these three examples give states the opportunity to impact on situations that take place beyond their national borders.

This book focuses on the third example, namely border tax adjustments (BTAs) in respect to internationally traded goods. The objective is to determine the extent to which countries may use such taxes to foster environmental goals at the international level. In other words, this book aims to demonstrate that it is legally possible to develop the environmental dimension of taxes imposed on internationally traded goods despite the legal limits that constrain countries in their design of border tax policies.

Both scholars and political figures have shown a growing interest in the potential role of border taxes to foster global environmental goals. This may be explained by the difficulties and limits in adopting ambitious environmental policies at the domestic level as well as the complexity in reaching international agreements on global environmental challenges.

In the literature, the concept of environmental BTAs is one of the most studied models of environmental tax imposed on internationally traded goods.\(^1\) The concept of BTAs – defined in 1968 by the Organisation for

\(^1\) The most significant works on environmental BTAs include: Madison Condon & Ada Ignaciuk, ‘Border Carbon Adjustment and International Trade. A
Economic Co-operation and Development (OECD) – reflects the idea that countries may both tax imported products in the same way as they tax domestic ‘like’ products and relieve exported products from domestic taxes. The concept of environmental BTAs has been developed in the scholarship as a legal instrument to mitigate cross-border environmental issues, usually based on a two-fold rationale, both economic and political. First, in contrast to domestic environmental policies that only apply to domestic products and domestic producers, environmental BTAs apply to internationally traded goods and are therefore supposed to limit the risks of loss of competitiveness and pollution leakage. Second, environmental BTAs – which may be adopted unilaterally as opposed to international agreements – would be politically sound in that they could encourage third countries to follow suit by adopting new environmental standards at the domestic level. No consensus exists, however, in the economic literature on the validity of these arguments and on the exact effects of environmental BTAs. This book does not take a stance on the
validity of this literature, which is only used as an element of factual background.

In addition to their differences with pure domestic and international legal instruments, environmental border taxes should also be distinguished from ‘non-economic (border) regulations’. First, regulations may be formulated in terms of voluntary standards, such as labelling requirements to provide consumers with better information on the environmental impact of the products that they consume. In contrast to such labelling instruments, taxes are a more direct tool to internalise the cost of pollution into products’ prices. Second, regulations can serve to ban access to products that do not meet certain environmental standards. In contrast, taxes and other market-based instruments offer more possibilities for integrating environmental considerations into internationally traded goods.\(^3\) With non-market-based regulations, the legislator may choose between two possibilities: to ban or not to ban the products. With taxes, the legislator has the same two possibilities: to impose a tax or not to impose a tax. However, the possibility of imposing a tax offers more alternatives than a ban. For example, the legislator may impose differentiated taxes, with different tax rates based on the environmental impact of the products.

This book aims to analyse environmental BTAs from a three-fold perspective, referring to the rationale of BTAs, their tax design and their legal framework.

Despite the highly political character of border taxation, the literature only contains a few references to the history and rationale of taxes imposed on internationally traded goods. However, the analysis of the rationale behind border taxes is key to determining the extent to which traditional BTAs allow the pursuit of environmental goals. The reason for this key role relates to the fact that the main legal provisions surrounding traditional BTAs have been drafted taking into consideration the objectives that these measures were aimed at pursuing. In other words, analysis of the rationale underlying traditional models of BTAs allows us to better understand the extent to which such tax models may be compatible with – and even integrate – environmental considerations (Part I). Academic literature appears fragmented: various tax and international trade law

\(^3\) Quota restrictions could also serve to exert pressure on non-environmentally friendly countries to adopt environmental policies. Such measures would, however, be unlikely to comply with WTO law.
concepts are used inconsistently. Though legal concepts may be appealing from a rhetorical viewpoint, the inconsistent use of legal terms makes the literature confusing. Indeed, when a policy measure is mistakenly named after a legal concept, the legal analysis that follows will also be wrong.

Moreover, the legal scholarship has not yet analysed in detail the tax design of environmental BTAs. The analysis of the tax design of such taxes is nevertheless necessary to assessing how – and to what extent – environmental criteria could be integrated into traditional BTAs, taking account of the practical implementation of these taxes. Therefore, the analysis explains how BTAs are designed by means of illustrative examples such as the EU VAT and excise duties systems and the US sales tax (Part II). Analysis of the design of BTAs is largely based on practical questions: ‘How are these taxes applied in practice?’; ‘How could environmental criteria be included in their tax mechanism?’; ‘Should the tax rate be modulated based on environmental factors?’; ‘Should the tax only be imposed on polluting products?’, etc.

Finally, regarding the legal framework of BTAs, the academic literature has mainly focused its attention on the World Trade Organization (WTO) law compatibility of environmental BTAs. This research looks beyond WTO law’s mainstream interpretations and highlights that WTO law provisions surrounding (environmental) BTAs may be interpreted in such a way to permit their development (Part III). The approach is inspired by Critical Legal Studies, a movement that considers that law is ‘indeterminate’ and intrinsically linked to politics. Based on this critical approach, this book highlights the conflicting views on the legal provisions

4 Few tax scholars have analysed the interactions between tax and WTO law. See Jennifer E. Farrell, The Interface of International Trade Law and Taxation (26 IBFD Doctoral Series 2013); Michael Lang, Judith Herdin & Ines Hofbauer (eds.), WTO and Direct Taxation (Linde Verlag 2005); Michael Lang, Judith Herdin-Winter & Ines Hofbauer-Steffel (eds.), The Relevance of WTO Law for Tax Matters (Linde Verlag 2006); Marilyne Sadowsky, Droit de l’OMC, droit de l’Union européenne et fiscalité directe (Larcier 2013).

5 This research nevertheless acknowledges the argument that a dispute settlement body is unlikely to distance itself from interpretations considered to be mainstream.

surrounding environmental BTAs and demonstrates that room exists for supporting their adoption. Consequently, it argues that the alleged incompatibility of environmental BTAs with international (trade) law cannot serve as a legal excuse not to adopt environmental policies at the national level.

Ultimately, this book seeks to bring some coherence to the legal literature, which is – given the interdisciplinary nature of the topic – necessarily a little chaotic.8


Westin introduced his book with a similar idea. He wrote as follows:

This writer cannot hope to do more than to raise the level of confusion. The reason is that this work covers numerous subjects: international trade treaties, microeconomics, tax policy concepts, and environmental taxes. None of these subjects is tidily stowed away. When one combines them, the outcome can only be organized chaos. Still, there is need for the study, because the pressures are urgent.

(Westin, supra n. 1)