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THE EUROPEAN UNION CARBON BORDER ADJUSTMENT MECHANISM: COMPATIBILITY WITH WTO LAWS AND IMPLICATIONS FOR FTAS

DR. PRALOK GUPTA* & DR. SHAGUFTA NAAZ**

The European Union's (EU) Carbon Border Adjustment Mechanism (CBAM) entered its definitive phase on January 01, 2026, becoming the first operational border carbon adjustment instrument adopted by a major economy. The Regulation extends the carbon price signal of the EU Emissions Trading System (EU ETS) to imports of cement, electricity, fertilisers, iron and steel, aluminium and hydrogen, with a planned downstream extension from January 2028. This paper analyses the existing literature that examines whether CBAM is compatible with the multilateral disciplines of the World Trade Organization (WTO) and how the EU's network of Free Trade Agreements (FTAs) interacts with this measure. The paper finds that several design features of CBAM are likely to violate the national treatment obligation under Article III:4 and the Most Favoured Nation (MFN) obligation under Article I:1 of the General Agreement on Tariffs and Trade (GATT). The General Exceptions in Article XX may be available to the EU but the chapeau is a demanding test, and that the enabling clause provides a doctrinal basis for differentiated treatment that the EU has chosen not to use. The paper further finds that the EU's FTAs may not legally exempt partners from CBAM without violating the MFN obligation, and that the most of these FTAs can offer is procedural cooperation.

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I. INTRODUCTION

Climate policy and trade policy have circled each other for more than three decades without ever fully meeting. Since the United Nations Framework Convention on Climate Change (UNFCCC) opened for signature in 1992 and the WTO came into operation in 1995, the international system has carried two parallel architectures, one for emissions reduction and another for trade liberalisation.[1] These architectures were built by different communities of negotiators, on different premises, and with different mandates. The climate regime accepted from the outset that historical responsibility for greenhouse gas emissions varied across states, and built differentiation into the very text of the Convention through the principle of 'common but differentiated responsibilities and respective capabilities'.[2] The trade regime, by contrast, was designed around the principle of non-discrimination in its 'national treatment' and 'most-favoured nation' forms, with carefully limited exceptions for environmental and other public interest measures.[3]

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[1] United Nations Framework Convention on Climate Change, May 9, 1992, 1771 U.N.T.S. 107 [hereinafter UNFCCC]; Marrakesh Agreement Establishing the World Trade Organization, Apr. 15, 1994, 1867 U.N.T.S. 154 [hereinafter WTO Agreement].
[2] UNFCCC, *supra* note 1, art. 3(1); *see also* LAVANYA RAJAMANI, DIFFERENTIAL TREATMENT IN INTERNATIONAL ENVIRONMENTAL LAW (2006).
[3] General Agreement on Tariffs and Trade 1994, arts. I, III and XX, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 U.N.T.S. 190 [hereinafter GATT 1994].

In this regard, the CBAM may be considered as the most consequential attempt to date to bring these two architectures into operative contact. Adopted as Regulation (EU) 2023/956 of the European Parliament and of the Council on May 10, 2023, CBAM extends the carbon price of the EU ETS to a defined set of imports.[4] Its transitional phase ran from October 01, 2023 to December 31, 2025 and its definitive phase began on January 01, 2026. The objective is to put a fair price on the carbon emissions produced while manufacturing carbon intensive goods that are imported into the EU. Further, it aims at encouraging cleaner industrial production through an embedded emissions methodology. From that date, importers of iron and steel, aluminium, cement, fertilisers, hydrogen and electricity from specific third countries must hold and surrender CBAM certificates corresponding to the embedded emissions of the imported goods, with the certificate price tied to the weekly auction price of EU ETS allowances.[5] The EU has presented CBAM as a measure necessary to prevent carbon leakage and to support the credibility of European climate policy. The EU's trading partners have responded with a mixture of cautious acceptance, technical engagement, and open opposition while several have raised formal concerns at the WTO.[6]

The question of whether CBAM is compatible with WTO disciplines is the most important legal question which is central to its long-term viability. It is also a question that is not yet answered in the WTO jurisdiction. No panel has yet been established to examine CBAM, and the dispute settlement system is in any case operating under the constraint imposed by the United States blockage of new appointments to the Appellate Body.[7] The European Court of Justice has not been called upon to consider the WTO consistency of the Regulation, and in any event has consistently denied direct effect to WTO law within the European legal order.[8] The legal analysis must therefore proceed on the basis of the architecture of the Regulation, the text of the GATT and related instruments, the case law of WTO

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[4] Regulation (EU) 2023/956 of the European Parliament and of the Council of 10 May 2023 establishing a Carbon Border Adjustment Mechanism, 2023 O.J. (L 130) 52 [hereinafter CBAM Regulation].
[5] *Id.*, arts. 4, 21 and 22; *see also Id.,* Annex I and Annex III.
[6] World Trade Organization, *Minutes of the Meeting of the Council for Trade in Goods 30 April-1 May, 2024*, ¶ 7, WTO Doc. G/C/M/148 (June 13, 2024) [hereinafter WTO Doc. G/C/M/148].
[7] *See* Joost Pauwelyn, *WTO Dispute Settlement Post 2019: What to Expect?*, 22(3) J. INT'L ECON. L. 297 (2019).
[8] Case C-149/96, Portuguese Republic v. Council of the European Union, 1999 E.C.R. I-08395, ECLI:EU:C:1999:574 [hereinafter Portuguese Republic v. Council of the EU].

panels and the Appellate Body, and the substantial academic literature that has grown around the measure.[9]

A second, related question is how CBAM interacts with the EU's existing and future FTAs. CBAM is a measure of general application that the FTAs do not, and probably cannot, override without raising the same most-favoured nation problems as the Regulation itself.

In this context, this paper presents the findings of various studies on the EU CBAM and addresses two interlinked questions. First, if the CBAM is compatible with the multilateral disciplines of the WTO, and if not, what are the specific points of inconsistency? Second, how does CBAM interact with the EU's free trade agreement practice, and what policy space do FTA partners have in the context of CBAM? The paper proceeds in four substantive sections after this introductory section, examining CBAM's design, its WTO compatibility, its interaction with FTAs, and the concluding thoughts with some policy implications.

II. CBAM: ORIGIN, EVOLUTION, REGULATION, AND IMPLEMENTATION

CBAM is a piece of EU climate legislation that places a price on the carbon emissions embedded in certain goods imported into the Union. In simple terms, it works as a charge that mirrors what European producers already pay under the EU ETS when they release greenhouse gases inside the bloc.[10] If a steel mill in Germany must pay for every tonne of carbon dioxide it emits, then a steel mill in another country selling to the same European market should not enjoy a free ride simply because it operates outside Europe. CBAM seeks to remove this asymmetry. The legal instrument that gives effect to this idea is Regulation (EU) 2023/956, published in the Official Journal on May 16, 2023.[11]

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[9] For leading treatments, *see* Michael A. Mehling et al., *Designing Border Carbon Adjustments for Enhanced Climate Action*, 113(3) AM. J. INT'L L. 433 (2019) [hereinafter Mehling]; Gary Clyde Hufbauer et al., *Can EU Carbon Border Adjustment Measures Propel WTO Climate Talks?*, PETERSON INST. FOR INT'L ECON. 21, 21–23 (2021), https://www.piie.com/sites/default/files/documents/pb21-23.pdf [hereinafter Hufbauer]; James Bacchus, *Legal Issues with the European Carbon Border Adjustment Mechanism* (Cato Inst., Briefing Paper No. 125, 2021), https://www.cato.org/briefing-paper/legal-issues-european-carbon-border-adjustment-mechanism [hereinafter Bacchus].
[10] CBAM Regulation, *supra* note 4, art. 1; Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a Scheme for Greenhouse Gas Emission Allowance Trading within the Community and amending Council Directive 96/61/EC, 2003 O.J. (L 275) 32 [hereinafter ETS Directive] (as amended).
[11] CBAM Regulation, *supra* note 4, Preamble.

A. The Origin of CBAM

To understand why the EU introduced such a measure, it is necessary to look at the broader story of European climate policy and an old problem that has troubled it for years, namely carbon leakage. Carbon leakage refers to the situation where stricter climate rules in one jurisdiction push polluting industries to relocate to places with weaker rules, or where domestic producers lose market share to foreign competitors who do not bear the same carbon costs.[12] The result is that the climate rules of the stricter jurisdiction succeed only on paper. From the European point of view, this defeats the purpose of the EU ETS, which has been the cornerstone of European climate policy since 2005.[13]

The EU ETS works on a cap-and-trade basis. It places a limit on how much carbon dioxide and certain other greenhouse gases industrial installations within Europe may emit. Installations must surrender allowances equal to their actual emissions, and these allowances trade in a market where the price reflects scarcity.[14] To address carbon leakage, the European Union granted free allowances to industries considered most exposed, such as cement, steel, aluminium and certain chemicals.[15] But free allowances came with their own difficulty: they blunted the very price signal that the EU ETS was supposed to send. The European Commission, therefore, began to look for an alternative. As an alternative, instead of shielding domestic producers from carbon costs, it sought a way to extend those costs to imports.[16]

The political momentum for CBAM came together with the European Green Deal, presented by the Von der Leyen Commission in December 2019, which set the goal of climate neutrality by 2050 and committed the EU to reduce net greenhouse gas emissions by at least 55% by 2030 compared with 1990 levels.[17] The Fit for 55

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[12] *See Carbon Leakage*, EUROPEAN COMMISSION, https://climate.ec.europa.eu/eu-action/eu-emissions-trading-system-eu-ets/free-allocation/carbon-leakage_en; Michael Grubb et al., *Carbon Leakage, Consumption, and Trade*, 47 ANN. REV. ENV'T & RES. 753 (2022).
[13] A. Denny Ellerman & Barbara K. Buchner, *The European Union Emissions Trading Scheme: Origins, Allocation, and Early Results*, 1(1) REV. ENV'T. ECON. & POL'Y 66 (2007).
[14] ETS Directive, *supra* note 10, arts. 9–12.
[15] Frank J. Convery, *Reflections—The Emerging Literature on Emissions Trading in Europe*, 3(1) REV. ENV'T. ECON. & POL'Y 121 (2009); Misato Sato et al., *Allocation, Allocation, Allocation! The Political Economy of the Development of the European Union Emissions Trading System*, 13(5) WILEY CLIMATE CHANGE 1 (2022).
[16] Stefan Ambec et al., *The Economics of Carbon Leakage Mitigation Policies*, 125 J. J. ENV'T. ECON. & MGMT. 102973 (2024); Mehling, *supra* note 9.
[17] *The European Green Deal*, COM (2019) 640 final (Dec. 11, 2019).

package of July 2021 translated this commitment into a legislative programme, and CBAM was one of its central pieces.[18]

B. The Legislative Evolution and Structure

The Commission tabled its formal proposal on July 14, 2021. The Parliament adopted its position in June 2022, and the Council reached its general approach in March 2022. After the trilogue process, a provisional political agreement was reached in December 2022, and the final text was adopted as Regulation (EU) 2023/956 on May 10, 2023, entering into force on May 17, 2023.[19] The Regulation sets out the broad architecture, but the technical and operational rules have been filled in through implementing acts, the most important of which is Commission Implementing Regulation (EU) 2023/1773 of August 17, 2023, laying down the rules for the application of CBAM during its transitional period.[20]

The Regulation runs to 36 articles and 8 annexes. Article 1 states that CBAM applies to imports of certain goods listed in Annex I and that it works by requiring importers to surrender CBAM certificates corresponding to the embedded greenhouse gas emissions of those goods. The price of each certificate tracks the weekly average auction price of EU ETS allowances.[21] Annex I covers six categories of goods: cement, electricity, fertilisers, iron and steel, aluminium and hydrogen, along with certain downstream products derived from iron and steel and aluminium.[22] According to Commission estimates, when fully implemented, these sectors will account for more than half of the emissions from industrial sectors covered by the EU ETS.[23]

Annex III lists the territories exempt from CBAM because they participate in the EU ETS or operate a fully linked national emissions trading system, namely, Iceland,

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[18] *'Fit for 55': delivering the EU's 2030 Climate Target on the way to climate neutrality*, COM (2021) 550 final (July 14, 2021).

[19] *Proposal for a Regulation of the European Parliament and of the Council: Establishing a Carbon Border Adjustment Mechanism*, COM (2021) 564 final (July 14, 2021) [hereinafter COM (2021)]; CBAM Regulation, *supra* note 4, art. 36.

[20] Commission Implementing Regulation (EU) 2023/1773 of 17 August 2023 Laying Down the Rules for the Application of Regulation (EU) 2023/956 of the European Parliament and of the Council as regards Reporting Obligations during the Transitional Period, 2023 O.J. (L 228) 94 [hereinafter Implementation Regulation 2023/1773].

[21] CBAM Regulation, *supra* note 4, arts. 1 and 21.

[22] *Id.*, Annex I.

[23] European Commission Press Release QANDA/21/3661, Carbon Border Adjustment Mechanism: Questions and Answers, (July 14, 2021) [hereinafter Press Release 21/3661].

Liechtenstein, Norway, and Switzerland, along with some smaller territories.[24] All other countries fall within scope, regardless of their level of development, a feature that lies at the heart of the WTO debate that follows. The greenhouse gases covered are carbon dioxide, nitrous oxide, and perfluorocarbons, with Annex I specifying which gases must be reported for which goods.[25] Direct emissions are those arising from the production process itself; indirect emissions are those from the generation of electricity consumed in production. For cement and fertilisers, both direct and indirect emissions are counted; for iron and steel, aluminium and hydrogen, only direct emissions are counted in the definitive period, subject to review under Article 30.[26]

CBAM and the EU ETS are linked by design. The price of a CBAM certificate is fixed each week by reference to the auction price of EU ETS allowances. The volume of CBAM certificates an importer must surrender is reduced in proportion to the free allowances still being granted to European producers in the same sectors.[27] As free allowances are phased out from 2026 to 2034, the volume of CBAM coverage grows. CBAM is, in this sense, a shadow extension of the EU ETS to the European border, framed by the Commission as a regulatory rather than fiscal obligation.[28] Figure 1 presents the evolution of CBAM in the European Union.

Figure 1: The Evolution of CBAM

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[24] CBAM Regulation, *supra* note 4, Annex III.
[25] *Id.*, art. 3 read with Annex I.
[26] *Id.*, arts. 3(22)–3(23) and 30(2).
[27] *Id.*, art. 31.
[28] *Carbon Border Adjustment Mechanism*, EUROPEAN COMMISSION, https://taxation-customs.ec.europa.eu/carbon-border-adjustment-mechanism_en.

December 13, 2022: Trilogue Agreement
Provisional political agreement reached between the three institutions.

May 10, 2023: Regulation (EU) 2023/956 Adopted
Final text adopted by the European Parliament and the Council; published in the Official Journal on 16 May 2023.

May 17, 2023: Regulation Enters into Force
CBAM becomes binding law across the European Union.

August 17, 2023: Implementing Regulation 2023/1773
Operational rules for the transitional period; further implementing and delegated acts to follow.

Source: Authors' construction based on various sources

C. How CBAM is Being Implemented

CBAM is being rolled out in two phases. The transitional phase ran from October 01, 2023 to December 31, 2025 whereas the definitive phase began on January 01, 2026.[29] The transitional phase was a learning period during which no financial obligation arose. Importers filed quarterly reports through the CBAM Transitional Registry, disclosing the quantity of CBAM goods imported, the actual embedded emissions, the indirect embedded emissions, and any carbon price already paid in the country of origin.[30] From January 01, 2025, only the EU-approved methodology for calculating embedded emissions has been acceptable, with default values permitted for complex goods only where they account for less than 20% of total embedded emissions.[31] Penalties between 10 and 50 Euros per tonne of unreported emissions have been applied since the beginning of the transitional phase.[32]

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[29] CBAM Regulation, *supra* note 4, arts. 32 and 36.
[30] *Id.*, art. 35; Implementation Regulation 2023/1773, *supra* note 20, Annex I.
[31] Implementing Regulation (EU) 2023/1773 *supra* note 20, art. 4 read with Annex III.
[32] CBAM Regulation, *supra* note 4, art. 16; Implementing Regulation (EU) 2023/1773, *supra* note 20, art. 16.

The definitive phase brings the financial obligation into operation. Only an authorised CBAM declarant may import goods listed in Annex I, with authorisation granted by the National Competent Authority of the Member State after a fifteen working day verification process. [33] Authorised declarants purchase CBAM certificates through a common central platform, with the price set weekly by reference to the EU ETS auction price. By the end of each quarter, the declarant must hold certificates equal to at least 50% of the embedded emissions of goods imported since the beginning of the calendar year, and by September 30 of each year must file an annual CBAM declaration covering the previous calendar year, supported by a verification report from an accredited verifier.[34] The first annual declaration falls due on September 30, 2027 and will cover 2026.[35]

The *de minimis* threshold for consignments was originally set at 150 Euros, but the Commission has since proposed and adopted amendments raising it to a mass based limit of 50 tonnes per importer per calendar year for most CBAM goods.[36] CBAM certificates are not tradable on an open market and have a limited life, with unused certificates automatically cancelled if not surrendered by June 30 of the year following purchase, and refunds capped at one third of certificates purchased during the previous year.[37] The carbon price already paid in the country of origin can be deducted from CBAM liability, but the deduction is limited to direct and explicit carbon pricing instruments, with implicit pricing not credited. [38] Where actual emissions data are unavailable, embedded emissions are calculated using default values drawn from the 10% least efficient European installations producing the same good.[39] The full burden of CBAM is being phased in over nine years, with free allowances under the EU ETS reduced gradually from 2.5% in 2026 to 100% by 2034.[40] Figure 2 presents the different phases of the implementation of CBAM.

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[33] CBAM Regulation, *supra* note 4, arts. 4 and 5.
[34] *Id.*, arts. 6, 8, 21, and 22.
[35] Regulation (EU) 2025/2083 of the European Parliament and of the Council amending Regulation (EU) 2023/956 as regards simplifying and strengthening the carbon border adjustment mechanism, 2025 O.J. (L 2025/2083) [hereinafter CBAM Simplification Regulation].
[36] *Id.*, art. 2(3); *Proposal Amending a Regulation of the European Parliament and of the Council Amending Regulation (EU) 2023/956 as regards simplifying and strengthening the Carbon Border Adjustment Mechanism*, COM (2025) 87 final (Feb. 26, 2025).
[37] CBAM Regulation, *supra* note 4, arts. 22, 23, and 24.
[38] *Id.*, art. 9.
[39] *Id.*, Annex IV.
[40] *Id.*, art. 36(3)(d); *see* Directive (EU) 2023/959 of the European Parliament and of the Council of 10 May 2023 Amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union and Decision (EU) 2015/1814

Figure 2: The Implementation of CBAM

Phase 1: Transitional Period (Oct. 01, 2023 – Dec. 31, 2025)
No financial obligation. Importers file quarterly reports only - quantities, embedded emissions (direct + indirect), and any carbon price already paid in the country of origin. First report due Jan. 31, 2024.

▼

Tightening of Methodology (from Jan. 01, 2025)
Only the EU-approved methodology is accepted. Estimates and default values are limited to complex goods and to less than 20% of total embedded emissions. Penalties of €10–€50 per tonne for missing or inaccurate reports.

▼

Phase 2: Definitive Period Begins (Jan. 01, 2026)
Financial obligation activated. Only an Authorised CBAM Declarant may import goods listed in Annex I (cement, electricity, fertilisers, iron & steel, aluminium, hydrogen and downstream products).

▼

Authorisation by National Competent Authority
Applicant verified (15 working days) on customs record, financial and operational capacity. Financial guarantee may be required. Non-EU importers must appoint an indirect customs representative.

▼

Purchase & Hold Certificates
Certificates bought on a central platform; price set by reference to the EU ETS auction price. By the end of each quarter, the declarant must hold certificates equal to at least 50% of the embedded emissions of goods imported since the beginning of the calendar year.

▼

Annual CBAM Declaration (by 30 September each year)

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concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading system, 2023 O.J. (L 130) 134.

Declarant files annual return for the previous calendar year - total goods, embedded emissions, certificates to surrender (net of carbon price paid abroad), and a verification report from an accredited verifier. First filing: September 30, 2027 for year 2026.

▼

Full Phase-in by 2034
EU ETS free allowances reduced progressively (2.5% in 2026 → 100% by 2034). CBAM coverage expands in proportion, until importers face the full EU carbon price at the border. Article 30 reviews may expand scope to new sectors.

Source: Authors' construction based on various sources

D. CBAM: What's Next?

Article 30 of the Regulation obliges the Commission to review the mechanism before the end of the transitional period and at regular intervals during the definitive period. The review must consider whether the scope should be extended to other goods at risk of carbon leakage, particularly organic chemicals, polymers, and downstream products that use CBAM goods as inputs, and whether indirect emissions and emissions from transport should be brought within the CBAM's scope.[41] The Commission has signalled clearly that the product scope will widen over time, and this evolutionary character matters for the analysis that follows.

Thus, though the scope of CBAM is limited to specific goods at present, however, this scope is likely to be expanded in future. Therefore, it becomes pertinent to analyse the compatibility of the EU CBAM with international trade laws. The questions of WTO compatibility and of implications for trading partners are not merely about the present narrow scope, rather, they are about a measure that may grow significantly in scope over the coming decade.

III. IS CBAM COMPATIBLE WITH WTO LAWS?

The European Commission has insisted at every stage of the legislative process that CBAM has been designed in a way so as to be fully compliant with WTO law. The premises to the Regulation state that the mechanism should be implemented in a

[41] CBAM Regulation, *supra* note 4, art. 30.

way that is consistent with international trade rules.[42] However, the EU's trading partners have been less convinced and countries such as India, China, Brazil, South Africa, Russia, Turkey and others have raised concerns at the WTO, and some have indicated that they are studying the possibility of bringing a formal dispute.[43] As of yet, no panel has been established to examine CBAM, but the legal arguments are on the table, and the academic debate has produced a substantial body of analysis.[44]

This section examines the WTO compatibility of CBAM in the order in which a panel would most likely approach the question. It addresses the legal characterisation of the measure under the GATT 1994, the obligations of national treatment under Article III, the MFN obligation under Article I, the general exceptions of Article XX with the chapeau, and the Enabling Clause as applied to developing country partners.

A. The WTO Framework and the EU's Position

The EU is itself a Member of the WTO, alongside its individual Member States, and Article XI:1 of the WTO Agreement records the European Communities (now the EU) as an original Member.[45] The European Commission represents the Union in WTO and the Directorate General for Trade negotiations and also litigates on its behalf, with exclusive competence over the Common Commercial Policy under the Lisbon Treaty.[46] The Union has been one of the most active users of the WTO dispute settlement system since 1995 and has been a strong advocate of the WTO and of its reform in light of the Appellate Body crisis.[47] At the same time, the European Court of Justice has consistently denied direct effect to WTO law within the European legal order, which means that EU institutions are not legally compelled by their own courts to bring an inconsistent measure into conformity, although political and reputational reasons remain compelling.[48]

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[42] COM (2021), *supra* note 19, at 10–11; *Id.*, recital 73.
[43] WTO Doc. G/C/M/148, *supra* note 6.
[44] Mehling, *supra* note 9; Hufbauer, *supra* note 9; Bacchus, *supra* note 9.
[45] WTO Agreement, *supra* note 1, art. XI:1.
[46] Consolidated Version of the Treaty on the Functioning of the European Union, art. 207, 2016 O.J. (C 202) 47; Treaty of Lisbon Amending the Treaty on European Union and the Treaty Establishing the European Community, Dec. 13, 2007, 2007 O.J. (C 306) 1.
[47] Igler Wolfgang, *The European Union and the World Trade Organization*, FACT SHEETS ON THE EUROPEAN UNION: EUROPEAN PARLIAMENT, 2 (2025); WITA: THE INTERNATIONAL TRADE ASSOCIATION, *EU Concept Paper: on WTO Reform*, (Sept. 2018), https://www.wita.org/atp-research/eu-concept-paper-on-wto-reform/.
[48] Portuguese Republic v. Council of the EU, *supra* note 8; Iva Živičnjak, *Effect of WTO Law in the EU and Individual's Right to Damages Caused by a Breach of WTO Law*, 8 CROATIAN Y.B. EUR. L. & POL'Y 531 (2012).

B. The Legal Characterisation of CBAM under the GATT

The first analytical step is to decide what kind of measure CBAM is, since different GATT disciplines apply to different categories. Three characterisations are plausible. First, CBAM could be a tariff or border charge, in which case Article II of the GATT applies and the measure would be a *prima facie* violation of Article II:1(b) since CBAM costs are not recorded in the EU's schedule of concessions.[49] Second, CBAM could be a quantitative restriction in disguise, with certificates operating as *de facto* import licences contrary to Article XI:1; this is the weakest of the three, since CBAM does not place an absolute ceiling on the quantity of imports.[50] Third, and most plausibly, CBAM could be a border adjustment of an internal regulation under Article II:2(a) read with Article III, an interpretation supported by the Note Ad Article III of the GATT and by the design of the Regulation itself.[51]

The European Commission has clearly designed CBAM with the third characterisation in mind. The price of certificates is fixed by reference to the EU ETS, the product scope mirrors the sectors covered by the EU ETS, and the volume of certificates is reduced in line with the free allowances still granted to European producers.[52] A panel, however, may not be bound by this self-characterisation. The WTO jurisprudence holds that the legal nature of a measure is determined by what it does, not by what its drafters say it is.[53] In *China — Measures Affecting Imports of Automobile Parts* case, the Appellate Body identified the trigger of the obligation as the key indicator—where the obligation is triggered by an internal event, the measure is internal, whereas triggered by importation, the measure is a border charge.[54] CBAM is not easy to classify on this test, since the obligation crystallises only at importation and there is no parallel internal obligation that applies to the embedded

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[49] GATT 1994, *supra* note 3, art. II:1(b); Ilaria Espa et al., *The EU Proposal for a Carbon Border Adjustment Mechanism (CBAM): An Analysis under WTO and Climate Change Law*, (World Trade Inst., WTI Working Paper No. 6, 2022), https://www.wti.org/media/filer_public/ee/61/ee6171fd-a68d-4829-875e-d9b0c32298b5/wti_working_paper_06_2022.pdf.

[50] GATT 1994, *supra* note 3, art. XI:1; Reinhard Quick, *Carbon Border Adjustment: A Dissenting View on its Alleged GATT Compatibility*, 4 ZEITSCHRIFT FÜR EUROPARECHTLICHE STUDIEN 549, 562 (2020) [hereinafter Quick]; Appellate Body Report, *China — Measures Related to the Exportation of Various Raw Materials*, ¶ 320, WTO Doc. WT/DS394/AB/R, WT/DS395/AB/R, and WT/DS398/AB/R (adopted Feb. 22, 2012).

[51] GATT 1994, *supra* note 3, art. II:2(a) and Note Ad Article III.

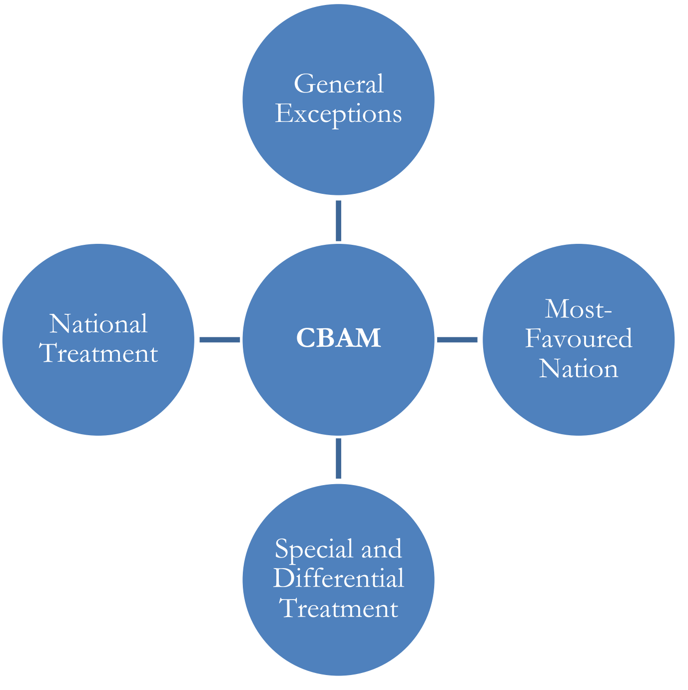
[52] CBAM Regulation, *supra* note 4, arts. 21 and 31.

[53] Appellate Body Report, *China — Measures Affecting Imports of Automobile Parts*, ¶¶ 159–164, WTO Doc. WT/DS339/AB/R, WT/DS340/AB/R, and WT/DS342/AB/R (adopted Jan. 12, 2009).

[54] CBAM Regulation, *supra* note 4, arts. 4, 6 and 22.

emissions of finished goods.[55] The analysis that follows proceeds on the assumption that CBAM is a border adjustment of an internal regulation, since that is the EU's position and the design depends on it. Figure 3 presents the possible interlinkages of CBAM with WTO disciplines.

Figure 3: Interlinkages of CBAM with WTO disciplines



Source: Authors' configuration

C. The National Treatment Obligation under Article III

If CBAM is a border adjustment of an internal regulation, the central discipline is the national treatment obligation in Article III. Article III:2 prohibits internal taxes on imported products in excess of those applied to like domestic products, while Article III:4 prohibits less favourable treatment under laws affecting their internal

[55] Quick, *supra* note 50; Joachim Englisch & Tatiana Falcao, *EU Carbon Border Adjustments for Imported Products and WTO Law*, SSRN, (2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3863038.

sale, purchase, transportation, distribution or use.[56] Article III:2 is more demanding; the European Court of Justice held in *Air Transport Association of America* case that the EU ETS is not a tax, since the cost of allowances is not fixed but follows the market price.[57] On that reasoning CBAM falls under Article III:4.

Under Article III:4, the first threshold question is likeness. The Appellate Body's classical likeness factors in *EC Asbestos* case are physical properties, end use, consumer tastes and habits, and tariff classification.[58] Process and production methods that do not affect the physical characteristics of the finished good have generally been treated as irrelevant to likeness.[59] On that test, two pieces of steel with the same chemistry and the same downstream use are like products even if produced with different carbon intensities.[60] No panel has yet adopted a more dynamic reading, and the more probable conclusion is that CBAM exposed imports and like domestic goods will be treated as like.

In the context of Article III:4, the second question is about less favourable treatment. The strongest objections to CBAM and its compatibility with WTO law lie on less favourable treatment. In this context, four design features have been identified in the literature as raising serious national treatment concerns. The first is the continuation of free allowances to European producers under the EU ETS, on a phase out schedule that reaches zero only in 2034.[61] The Regulation responds by reducing the volume of CBAM certificates required in proportion to the free allowances, but the calculation has been criticised as opaque and the result may still leave a gap between the effective carbon cost on European producers and on imports.[62]

The second is the asymmetric treatment of indirect emissions—the EU ETS does not regulate the indirect emissions of covered installations, while CBAM requires reporting and pricing of indirect emissions for cement and fertilisers, imposing a

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[56] GATT 1994, *supra* note 3, arts. III:2 and III:4.
[57] Case C-366/10, Air Transp. Ass'n of Am. v. Sec'y of State for Energy and Climate Change, 2011 E.C.R. I 13755, ¶¶ 142–144.
[58] *Border Tax Adjustments, Report of the Working Party*, L/3464, BISD 18S/97 (Dec. 02, 1970); Appellate Body Report, *European Communities — Measures Affecting Asbestos and Asbestos Containing Products*, ¶¶ 99–103, WTO Doc. WT/DS135/AB/R (adopted Apr. 05, 2001).
[59] Robert L. Howse & Donald H. Regan, *The Product/Process Distinction: An Illusory Basis for Disciplining 'Unilateralism' in Trade Policy*, 11(2) EUR. J. INT'L L. 249 (2000).
[60] Mehling, *supra* note 9.
[61] Alice Pirlot, *Carbon Border Adjustment Measures: A Straightforward Multi-Purpose Climate Change Instrument?*, 34(1) J. ENV'T. L. 25 (2022); Bacchus, *supra* note 9, at 3–5.
[62] Hufbauer, *supra* note 9.

higher effective burden on imports.[63] The third is the non-tradability of CBAM certificates. While European producers have access to a liquid secondary market for ETS allowances, the imported goods lack it, with refunds for excess CBAM certificates capped at one third of the previous year's purchase.[64] The fourth is the use of default values drawn from the 10% least efficient European installations, which can produce values far higher than the actual emissions of efficient producers in third countries and place the burden of proof on the exporter.[65]

The Appellate Body has held in *Korea Beef* case and elsewhere that less favourable treatment exists where the measure modifies the conditions of competition to the detriment of imports.[66] The *Dominican Republic Cigarettes* nuance allows that some negative effects on imports may be explained by factors unrelated to foreign origin.[67] The EU may try to argue that any disadvantage suffered by imports under CBAM flows from their carbon footprint and not from their foreign origin, but the four features described above do not flow from carbon footprint; they flow from the design of the regulatory regime itself, and they apply differently to imports than to like domestic products.[68]

D. The Most Favoured Nation Obligation under Article I

Article I:1 of the GATT requires that any advantage granted by a Member to any product originating in any other country be accorded immediately and unconditionally to like products from all other Members.[69] In the context of MFN, two features of CBAM raise concerns. The first is the carbon price credit, which is limited to direct and explicit carbon pricing instruments such as carbon taxes and emissions trading schemes; implicit carbon pricing such as fuel taxes, regulatory

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[63] CBAM Regulation, *supra* note 4, art. 7 read with Annex I; Arwel Davies, *The EU's Proposed Carbon Border Adjustment Mechanism and Compatibility with WTO Law*, 14(2) TRADE L. & DEV. 94, 102 (2022).
[64] CBAM Regulation, *supra* note 4, arts. 22 and 23; Press Release 21/3661, *supra* note 23.
[65] CBAM Regulation, *supra* note 4, Annex IV; Anatole Boute, *Accounting for Carbon Pricing in Third Countries Under the EU Carbon Border Adjustment Mechanism*, 23 WORLD TRADE REV. 168 (2024) [hereinafter Boute].
[66] Appellate Body Report, *Korea — Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, ¶ 137, WTO Doc. WT/DS161/AB/R and WT/DS169/AB/R (adopted Jan. 10, 2001) [hereinafter Korea Beef Case].
[67] Appellate Body Report, *Dominican Republic — Measures Affecting the Importation and Internal Sale of Cigarettes*, ¶ 96, WTO Doc. WT/DS302/AB/R (adopted May 19, 2005).
[68] Kateryna Holzer et. al., *The EU CBAM Proposal and WTO Law*, 13–8, (2022), https://www.bafu.admin.ch/dam/it/sd-web/6uYia0NKg2tc/rechtsgutachten-zur-einfuehrung-eines-co2-grenzausgleichsmechanismus-in-der-schweiz-annex-i.pdf.
[69] GATT 1994, *supra* note 3, art. I:1.

standards and energy efficiency mandates is not credited even though it imposes real economic costs.[70] The result is that two producers in two countries with similar climate ambition but different policy designs receive different treatment at the European border. The second concern is the binary character of the country exemption in Annex III—producers in countries with carbon pricing equivalent in effect but not identical in design are not extended the same treatment.[71]

E. General Exceptions under Article XX

Even if CBAM is found inconsistent with Article III or Article I, it can be saved if it qualifies under Article XX (General Exceptions), with the two most plausible heads being subparagraphs (b) and (g).[72] For fulfilling General Exceptions conditions, the Appellate Body has set out a two-step framework: the measure must first be provisionally justified under one of the listed paragraphs, then satisfy the chapeau.[73]

Article XX(b) covers measures necessary to protect human, animal or plant life or health.[74] Climate change is plainly capable of producing serious risks to human life, but the necessity test requires a serious examination of alternatives such as multilateral negotiation, climate finance and technology transfer.[75] Article XX(g) covers measures relating to the conservation of exhaustible natural resources, made effective in conjunction with restrictions on domestic production or consumption.[76] The Appellate Body in *US Gasoline* case accepted that clean air is an exhaustible natural resource, and in *US Shrimp* case adopted a broad reading of "relating to".[77] *US Shrimp* built on *US Gasoline* in two ways: it read "exhaustible natural resources" evolutively, extending Article XX(g) beyond mineral resources to living resources,

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[70] CBAM Regulation, *supra* note 4, art. 9; Boute, *supra* note 65, at 175–178.
[71] CBAM Regulation, *supra* note 4, Annex III; Appellate Body Report, *European Communities — Measures Prohibiting the Importation and Marketing of Seal Products*, ¶ 5.86–5.95, WTO Doc. WT/DS400/AB/R and WT/DS401/AB/R (adopted June 18, 2014).
[72] GATT 1994, *supra* note 3, art. XX (chapeau and subparagraphs (b) and (g)).
[73] Appellate Body Report, *United States — Standards for Reformulated and Conventional Gasoline*, ¶ 22, WTO Doc. WT/DS2/AB/R (adopted May 20, 1996) [hereinafter US Gasoline Case]; Appellate Body Report, *United States — Import Prohibition of Certain Shrimp and Shrimp Products*, ¶¶ 118–120, WTO Doc. WT/DS58/AB/R (adopted Nov. 06, 1998) [hereinafter US Shrimps Case].
[74] GATT 1994, *supra* note 3, art. XX(b).
[75] Korea Beef Case, *supra* note 66, at ¶ 166; Appellate Body Report, *Brazil — Measures Affecting Imports of Retreaded Tyres*, ¶ 156, WTO Doc. WT/DS332/AB/R (adopted Dec. 17, 2007) [hereinafter Brazil Retreaded Tyres Case].
[76] GATT 1994, *supra* note 3, art. XX(g).
[77] US Gasoline Case, *supra* note 73, at ¶ 14; US Shrimps Case, *supra* note 73, at ¶¶ 135–142.

and it recast "relating to" as a close and genuine relationship of ends and means between the measure and its conservation goal. The effect has been to lower the substantive threshold of Article XX(g) and to shift the real scrutiny to even-handedness and the chapeau. CBAM may clear these substantive thresholds without difficulty: the atmosphere's capacity to absorb greenhouse gases is an exhaustible natural resource on the logic of US Gasoline, the certificate obligation, calibrated to embedded emissions and priced by reference to the EU ETS, bears a close and genuine relationship to that conservation objective, and the EU ETS supplies the parallel restriction on domestic production. The harder question is the requirement of even handedness. The continued grant of free allowances to European producers blunts the domestic side of the bargain, and the use of default values that may overstate the emissions of efficient third country producers and thus tilts the burden away from the domestic side.[78]

The chapeau is where many environmental measures have failed.[79] In the *US Shrimp* case, the United States measure was provisionally justified under Article XX(g) but failed the chapeau because of arbitrary and unjustifiable discrimination, particularly through the unilateral imposition of a fixed regulatory programme on other Members without serious efforts at multilateral negotiation.[80] The CBAM may also be scrutinised on similar fronts. The carbon price credit draws an arbitrary distinction between explicit and implicit carbon pricing. The absence of any meaningful special and differential treatment for developing countries means that conditions in least developed countries (LDCs) and advanced industrial economies are treated identically. And the EU's offers of dialogue and technical assistance are modest in scale and lack a binding architecture.[81] The most realistic prediction is that CBAM might be provisionally justified under Article XX(g), and possibly under Article XX(b), but that several of its design features may fail the chapeau as currently drafted. The features most exposed are the recognition of only explicit carbon prices, the reliance on default values that efficient producers cannot easily displace, and the absence of differentiation for developing and least developed countries. As in US Gasoline, the remedy would be recalibration rather than abandonment: crediting implicit carbon pricing, easing recourse to verified actual emissions data,

[78] Sunayana Sasmal et. al., *Exempting Least Developed Countries from Carbon Border Adjustments: A Legal and Economic Analysis*, (Ctr. for Inclusive Trade Pol'y, CITP Briefing Paper No. 05, Oct. 04, 2023) [hereinafter Sasmal].
[79] US Shrimps Case, *supra* note 73, at ¶¶ 156–160; Brazil Retreaded Tyres Case, *supra* note 75, at ¶¶ 215–234.
[80] US Shrimps Case, *supra* note 73, at ¶¶ 161–170.
[81] Boute, *supra* note 65 at 180–184; Sasmal, *supra* note 78, at 12–16.

differentiating by development level, and undertaking genuine negotiation with affected exporters.[82]

F. The Enabling Clause and Special and Differential Treatment

A separate strand of WTO law that bears directly on CBAM is the Enabling Clause adopted in 1979.[83] Paragraph 2(a) covers preferential tariff treatment under the Generalized System of Preferences, paragraph 2(b) covers differential treatment in non-tariff measures, and paragraph 2(d) singles out LDCs for the most favourable treatment. Part IV of the GATT places parallel obligations on developed contracting parties to give priority to reducing barriers to products of interest to less developed contracting parties.[84] If CBAM is an internal regulation rather than a tariff, paragraph 2(b) provides a clear legal basis on which the EU could exempt LDCs or apply differentiated phase in periods.[85] The current Regulation does not provide such an exemption, applying uniformly to all third countries outside Annex III, including the least developed.[86] As Sasmal, Zhang, Lydgate and Winters have shown, the costs of CBAM compliance fall disproportionately on countries with thin export baskets and limited administrative capacity, and the resulting revenue transfer is hard to reconcile with the Common but Differentiated Responsibilities and Respective Capabilities principle.[87]

IV. CBAM AND THE EUROPEAN UNION'S FREE TRADE AGREEMENT PRACTICE

CBAM is a unilateral measure that does not require the consent of any FTA partner. The Regulation applies to all third countries other than those listed in Annex III, regardless of whether the country has an FTA with the EU.[88] Preferential tariff rates negotiated under each agreement continue to apply at the customs border but do not affect the obligation to surrender CBAM certificates. The MFN clauses in EU FTAs do not cure this gap, since they generally apply only to specific categories of

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[82] US Gasoline Case, *supra* note 73; World Trade Organization, *United States — Standards for Reformulated and Conventional Gasoline: Appellate Body Report and Panel Report: Action by the Dispute Settlement Body*, WTO Doc. WT/DS2/9, (May 20, 1996).
[83] *Differential and More Favourable Treatment Reciprocity and Fuller Participation of Developing Countries* (Nov. 28, 1979), GATT B.I.S.D. (26th Supp.) at 203(1979) [hereinafter Enabling Clause].
[84] GATT 1994, *supra* note 3, Part IV (arts. XXXVI–XXXVIII); Appellate Body Report, *European Communities — Conditions for the Granting of Tariff Preferences to Developing Countries*, ¶¶ 90–110, WTO Doc. WT/DS246/AB/R (adopted Apr. 20, 2004).
[85] Sasmal, *supra* note 78, at 14–16.
[86] CBAM Regulation, *supra* note 4, art. 2 read with Annex III.
[87] Sasmal, *supra* note 78, at 4–8.
[88] CBAM Regulation, *supra* note 4, art. 2 read with Annex III.

measures or incorporate the WTO MFN obligation by reference.[89] The dispute settlement provisions are also of limited use—an FTA partner that wishes to challenge CBAM on WTO grounds must do so through the WTO system, while a partner that wishes to challenge under the FTA must point to a specific FTA obligation that the Regulation breaches, and those obligations are difficult to identify.[90] Table 1 presents the mapping of EU FTA commitments with the provisions related to CBAM.

Table 1: Mapping of EU FTA Commitments and Provisions Related to CBAM

FTA	Concluded / Ratified	Chapter	Key Provisions	Relation to CBAM
EU-Australia FTA	March 24, 2026; ratification pending.	Chapter 18 - Trade and Sustainable Development.	Dedicated TSD chapter covering labour, gender equality, environment, climate and responsible business conduct; reaffirms the Paris Agreement and the ILO fundamental conventions.	No CBAM-specific provisions. Australia is not listed in Annex III of the CBAM Regulation, so Australian exports of CBAM goods to the EU are subject to the CBAM obligation.

[89] Comprehensive Economic and Trade Agreement (CETA) between Canada and the European Union, art. 8.7, 2017 O.J. (L 11) 23 [hereinafter Canada-EU CETA]; Agreement between the European Union and Japan for an Economic Partnership, art. 8.8, 2018 O.J. (L 330) 3 [hereinafter EU-Japan CETA].
[90] Canada-EU CETA, *supra* note 89, at ch. 29; Axel Marx et al., *Dispute Settlement for Labour Provisions in EU Free Trade Agreements: Rethinking Current Approaches*, 5(4) POL. & GOVERNANCE 49 (2017).

FTA	Concluded / Ratified	Chapter	Key Provisions	Relation to CBAM
			Parties commit to cooperate on climate-related matters including carbon pricing and the transition to a low-carbon economy. Zero tariffs on listed green goods from day one.	Cooperation on carbon pricing is foreseen as a soft-law avenue within the TSD chapter.
EU-India FTA	January 27, 2026; ratification pending.	Chapter 16 - Trade and Sustainable Development; ANNEX 14-A - Carbon Border Adjustment Measures.	Comprehensive TSD chapter: implementation of ratified MEAs (Paris Agreement, CBD, CITES), workers' rights based on the ILO fundamental conventions, women's empowerment, civil-society monitoring, and a right-to-regulate clause. Dedicated provisions on forest conservation,	This is the ONLY EU FTA so far that contains a dedicated CBAM annex (Annex 14-A). It does not exempt India from CBAM but provides a bilateral procedural and cooperation framework around CBAM implementation. Contained MFN treatment for any flexibilities the EU may

FTA	Concluded / Ratified	Chapter	Key Provisions	Relation to CBAM
			biodiversity, illegal wildlife trade, illegal logging and Illegal, Unreported, and Unregulated (IUU) fishing. Tariff reductions and services liberalisation for green goods and technologies.	grant other partners. Consistent with the EU position that an FTA cannot create a substantive CBAM carve-out.
EU-Indonesia CEPA	September 23, 2025; ratification pending.	Chapter 15 - Trade and Sustainable Growth and Development (TSGD); Protocol on Palm Oil.	TSGD chapter promotes environmental protection, climate action, workers' rights and women's empowerment, with a dedicated palm-oil platform. Parties commit to the effective implementation of the Paris Agreement, CBD and CITES, and to	No CBAM-specific provision as Indonesia is not in Annex III. Indonesian exports of CBAM goods face the full CBAM obligation. Cooperation on carbon pricing as embedded in the TSGD chapter.

FTA	Concluded / Ratified	Chapter	Key Provisions	Relation to CBAM
			cooperate on carbon pricing and the low-carbon transition. Zero tariffs on listed green goods from day one.	
EU-Chile Advanced Framework Agreement & Interim Trade Agreement (ITA)	ITA signed December 2023; entered into force February 01, 2025	Chapter 26 - Trade and Sustainable Development.	Modern TSD chapter aligned with the EU's 2022 'new approach': Paris Agreement implementation, binding commitments on labour rights based on ILO conventions, responsible business conduct, gender equality, sustainable food systems and trade in environmental goods. Transition to renewable	No CBAM-specific provision. Chile is not in Annex III; Chilean exports of CBAM goods (notably aluminium and fertiliser inputs) are subject to CBAM. Chile is rolling out a national carbon tax that, in principle, can be credited against the CBAM price under Article 9 of the CBAM Regulation, leaving exporters with only the

FTA	Concluded / Ratified	Chapter	Key Provisions	Relation to CBAM
			energy (such as lithium, copper, and renewable hydrogen) and sustainable use of raw materials.	residual difference between Chile's and the EU ETS price.
EU-Mercosur Partnership Agreement (EMPA) and Interim Trade Agreement (ITA)	Signed EMPA and ITA on January 17, 2026; ITA applies as of May 1, 2026; ITA will be repealed and replaced by EMPA once ratified.	Chapter 18 - Trade and Sustainable Development	TSD chapter reaffirming the Paris Agreement, the ILO fundamental conventions, sustainable forest management, biodiversity, CITES and responsible business conduct.	CBAM is *not* directly addressed. Mercosur countries (notably Brazil, a significant exporter of iron and steel and fertilisers to the EU) are subject to CBAM.
EU-Mexico Modernised Global Agreement	January 17, 2025; ratification pending.	Chapter 27 - Trade and Sustainable Development.	Updated TSD chapter aligned with the EU's 2022 'new approach': effective implementation of the Paris Agreement and ILO fundamental conventions,	No CBAM-specific provision. Mexico is not in Annex III. Mexican exports of CBAM goods (mainly steel and aluminium) are subject to CBAM.

FTA	Concluded / Ratified	Chapter	Key Provisions	Relation to CBAM
			sustainable management of forests and fisheries, circular-economy cooperation, trade in environmental goods and services, and responsible business conduct.	Mexico is developing a national ETS (currently in pilot phase) whose price is below the EU ETS, so producers face the residual CBAM cost.
EU-UK Trade and Cooperation Agreement (TCA)	Signed December 30, 2020; in force May 01, 2021.	Title XI - Level Playing Field for Open and Fair Competition and Sustainable Development; Chapter 7 - Environment and Climate.	Robust level-playing-field architecture: non-regression clauses on labour, environment, climate and subsidies, and a commitment under Article 392(6) to maintain effective carbon pricing covering greenhouse-gas emissions from electricity generation, industry,	UK is not in Annex III, so UK exports of CBAM goods to the EU are subject to CBAM. The UK is introducing its own CBAM from January 01, 2027. Article 392(6) and the joint declaration on carbon pricing provide the legal scaffolding for possible mutual recognition or

FTA	Concluded / Ratified	Chapter	Key Provisions	Relation to CBAM
			aviation and heat generation. Cooperation on linking respective carbon-pricing systems is explicitly foreseen.	price equivalence; negotiations on linking the EU ETS and UK ETS are under way but no binding outcome has been reached.
EU-Vietnam FTA (EVFTA)	Signed June 30, 2019; in force August 01, 2020.	Chapter 13 - Trade and Sustainable Development.	First-generation 'new template' TSD chapter: commitments to ILO fundamental conventions, effective implementation of MEAs including the Paris Agreement, sustainable forest management, etc.	No CBAM-specific provision as Vietnam is not in Annex III. Vietnam has no operational domestic carbon-pricing system, so Vietnamese producers of CBAM goods currently face the *full* CBAM cost.
EU-Canada Comprehensive Economic and Trade Agreement (CETA)	Signed October 30, 2016; provisionally applied since September 21, 2017;	Chapter 22 - Trade and Sustainable Development; Chapter 24 - Trade and Environment.	Chapter 24 reaffirms the parties' commitments under multilateral environmental agreements,	No CBAM-specific provision. Canada is not in Annex III. Canada has a robust federal carbon-pricing

FTA	Concluded / Ratified	Chapter	Key Provisions	Relation to CBAM
	full ratification pending in some EU Member States.		including the Paris Agreement, and promotes cooperation on climate policy, including emissions trading. Standard MFN clause (Article 8.7).	benchmark (Greenhouse Gas Pollution Pricing Act 2018) supplemented by provincial schemes.
EU-Switzerland Agreement on Linking the Emissions Trading Systems	Signed November 23, 2017; in force January 01, 2020.	Stand-alone agreement (not an FTA chapter); operates alongside the 1973 EU-Switzerland Free Trade Agreement and bilateral agreements.	Provides for the full linking of the EU ETS and the Swiss ETS: mutual recognition of allowances, common rules on auctioning, monitoring, reporting, verification and compliance. To date this is the only operational example of full ETS linkage with the European Union.	Switzerland is *listed in* ANNEX III of the CBAM Regulation and is therefore exempt from CBAM in respect of its exports to the EU. The exemption is rooted in the ETS linkage, not in the FTA.

Source: Authors' construction based on various FTA texts

A look at several of the EU's most important FTAs illustrates how CBAM reshapes the bilateral picture. The EU and United Kingdom Trade and Cooperation Agreement is unique because it followed the United Kingdom's withdrawal from the European Union and contains a robust level playing field chapter committing both parties to effective carbon pricing.[91] The United Kingdom has adopted its own CBAM scheduled from January 01, 2027, and the prospect of mutual recognition or carbon price equivalence is being explored but has not yet produced a binding outcome.[92]

The Comprehensive Economic and Trade Agreement with Canada has been provisionally applied since 2017 and contains Trade and Sustainable Development and Trade and Environment chapters reaffirming Paris commitments.[93] Canada has its own carbon pricing system at the federal level, supplemented by provincial schemes, and is a useful test case for how the CBAM credit will work in practice.[94]

The agreements with Japan and Korea contain Trade and Sustainable Development chapters with references to the Paris Agreement, and Korea's emission trading scheme generates a market price below the EU ETS price, with Korean producers facing a residual CBAM cost equal to the difference.[95] The FTA with Vietnam, in force since 2020, was concluded under the new generation template, but Vietnam

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[91] Trade and Cooperation Agreement between the European Union, the European Atomic Energy Community, and the United Kingdom of Great Britain and Northern Ireland, art. 392(6), 2021 O.J. (L 149) 10.

[92] HM Treasury & Dep't. for Energy Sec. and Net Zero, Consultation Outcome: Factsheet: UK Carbon Border Adjustment Mechanism, no. 2, (Dec. 18, 2023), https://www.gov.uk/government/consultations/addressing-carbon-leakage-risk-to-support-decarbonisation/outcome/factsheet-uk-carbon-border-adjustment-mechanism#:~:text=The%20UK%20CBAM%20will%20place,subject%20of%20consultation%20in%202024.

[93] Canada-EU CETA, *supra* note 89, at chs. 22 and 24.

[94] Greenhouse Gas Pollution Pricing Act, S.C. 2018, c. 12, s. 186, (Can.); Government of Canada & Dep't. of Fin., *Exploring Border Carbon Adjustments for Canada*, (Aug. 05, 2021), https://www.canada.ca/en/department-finance/programs/consultations/2021/border-carbon-adjustments/exploring-border-carbon-adjustments-canada.html.

[95] EU-Japan CETA, *supra* note 89, at art. 16.4; Free Trade Agreement between the European Union and its Member State, of the one part, and the Republic of Korea, of the other part, art. 13.5, 2011 O.J. (L 127) 6; Int'l. Carbon Action Partnership, *Korea Emissions Trading System (K-ETS)*, (2025), https://icapcarbonaction.com/en/ets/korea-emissions-trading-system-k-ets.

has no domestic carbon pricing system and Vietnamese producers face the full CBAM cost.[96]

The EU and Mercosur Agreement was finally concluded in late 2024 with an additional instrument on climate, biodiversity and labour, but CBAM was not directly addressed.[97] Switzerland is exempt from CBAM under Annex III because its emission trading system has been linked to the EU ETS since 2020, and remains the only currently operational example of full linkage.[98] The European Union and United States Global Arrangement on Sustainable Steel and Aluminium, launched in 2021, was an attempt to construct a transatlantic regime addressing both carbon intensity and overcapacity, but did not reach a binding outcome.[99]

An FTA cannot exempt a partner from CBAM in respect of its general application, since the exemption would discriminate among third countries and thus, violate Article I of GATT.[100] An FTA cannot modify the EU ETS, and it cannot reduce the price of CBAM certificates for the partner without raising the same Article I problem. The EU has been firm on these points, rooted in the Article I analysis discussed in Section 3.[101] What this means is that the most a partner can expect from an FTA is a procedural and cooperative arrangement around CBAM, not a substantive carve-out.

V. CONCLUSION

The CBAM is the most important new instrument that the EU has added to its trade and climate policy in a generation. Its design draws on more than a decade of European policy thinking about how to extend the price signal of the EU ETS to

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[96] Free Trade Agreement Between the European Union and the Socialist Republic of Vietnam, ch. 13, 2020 O.J. (L 186) 1; Rajeev Kher & Anshuman Gupta, *EU CBAM: Trade Implications and Policy Responses*, 6 (RIS Pol'y Brief, Pollicy Brief No. 128, Jan. 2026).

[97] European Commission Press Release IP/19/3396, European Commission Press Release IP/19/3396, EU and Mercosur Reach Agreement on Trade (June 28, 2019); Annex 18-A to Trade and Sustainable Development ch. 18, EU-Mercosur Partnership Agreement, (Dec. 06, 2024), https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-and-regions/mercosur/eu-mercosur-agreement_en.

[98] CBAM Regulation, *supra* note 4, Annex III; Agreement Between the European Union and the Swiss Confederation on the Linking of their Greenhouse Gas Emissions Trading Systems, 2017 O.J. (L 322) 3.

[99] European Commission Press Release IP/21/5724, Joint EU-US Statement on a Global Arrangement on Sustainable Steel and Aluminium (Oct. 31, 2021).

[100] GATT 1994, *supra* note 3, art. I:1.

[101] European Commission Statement/25/643, Joint Statement on the Second Meeting of the EU-India Trade and Technology Council, (Feb. 28, 2025).

imports. Its operation will, over the next decade, reach into a steadily widening range of goods and through them into the manufacturing economies of most of the EU's major trading partners. The argument advanced in this paper has been that CBAM is a serious legal instrument with serious legal problems and that those problems cannot be cured by the EU's network of FTAs.

The analysis has shown that several design features of CBAM produce treatment differences that do not flow from carbon footprint but from the architecture of the regulatory regime itself. The continuation of free allowances during the phase in period, the asymmetric treatment of indirect emissions, the non-tradability of CBAM certificates, the use of default values based on the 10%least efficient European installations, and the limited scope of the carbon price credit are vulnerable under Article III:4 of the GATT. The binary character of the country exemption in Annex III and the narrow definition of the carbon price credit raise concerns under Article I:1 of GATT. Whereas, the general exceptions in Article XX(b) and Article XX(g) are likely to be available, but the chapeau is a more demanding test, and the absence of meaningful differentiation in favour of developing countries is a serious obstacle. The Enabling Clause provides a doctrinal basis on which differentiation could be incorporated, and it is striking that the EU has chosen not to use that flexibility.

The FTA analysis has shown that the EU's network of agreements provides a sophisticated architecture for managing bilateral trade relationships, but that CBAM sits inside that architecture as a measure of general application that the FTAs do not, and probably cannot, override. The most that an FTA can offer is procedural cooperation, technical assistance and a soft commitment to consider the partner's compliance efforts. The post CBAM template, with Paris Agreement compliance treated as an essential element and the Trade and Sustainable Development chapter brought into enforceable dispute settlement, deepens the climate dimension but does not deliver substantive relief from CBAM. The carbon club idea may eventually provide coordination among countries with comparable carbon prices, but it carries the risk of entrenching a two-tier system.

Lastly, CBAM will not be the last measure of its kind. The United Kingdom's CBAM is scheduled to come into operation on January 01, 2027, and Canada, Australia and Japan are studying similar instruments. As more economies adopt their own border carbon adjustments, the case for some form of multilateral coordination, whether through the WTO, through the United Nations climate regime or through a carbon club arrangement, will become harder to resist. For developing and least developed countries, the stakes are high. Uncoordinated schemes multiply reporting and verification burdens across regimes, fall hardest on exporters with limited administrative capacity, sit uneasily with the principle of common but differentiated responsibilities, and risk setting standards in forums where those countries have no voice. Multilateral coordination offers the only route by which common accounting standards, mutual recognition and differentiated treatment can be built into the architecture from the outset.