

## Climate Club: The Way Forward

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### Origins of the idea

A Climate or Carbon Club has been proposed as a form of cooperation which could be established between like-minded countries sharing ambitious climate policies to encourage all others to follow suit and embark on equally grand climate measures. For the time being, this is a rather amorphous idea which needs to be converted into an effective instrument of the global climate transition. It remains unclear who could form a club, how its members could organise cooperation, what conditions would be expected from those willing to join, and what kind of instruments members could use to achieve their club's aims.

The theoretical concept of a Climate Club was initially outlined by [William Nordhaus](#), who saw it as a tool to overcome free-riding in international climate policy and ensure the global adoption of climate measures. In his view, countries with the ambition to undertake the costly action of putting a price on carbon emissions should form such a club and use international trade as a mechanism to impose on all those unwilling "free-riders" the cost of their contribution to global warming. In Nordhaus' original proposal, the focus was put on a group of large, economically advanced countries who were emitters of greenhouse gas (GHG) and ready to run ambitious climate policies, incentivising the rest of the world to follow suit. The Climate Club could then easily be enlarged as many other countries would prefer joining to avoid additional costs. The idea of forcing the hand of climate laggards is attractive, as negotiations in the UN platform are time-consuming, inefficient, and deliver minuscule outcomes at a time of climate urgency. Frustratingly, it took nearly three decades of negotiations and over twenty global ministerial meetings of

the United Nations Framework Convention on Climate Change (UNFCCC) before the Paris Agreement was agreed. Seven years after the Agreement's adoption, its [effects on stepping up global climate action can hardly be seen](#).

As [Bruegel](#) researchers recently noted, now is probably the best time to think about creating a Climate Club. But even if conditions are better than they were previously, the creation of such a "Club", which would affect every country of the world and require of them climate action more demanding than the Paris Agreement and UNFCCC, can be difficult to materialise. Its creation might encounter many problems, as there are few countries of similar ambition levels enforcing similar climate policies that could easily become the founders of such a group. Potential members might have different levels of ambition and diverging priorities in their climate action, and might use a variety of tools to achieve a reduction of their GHG emissions. Importantly, founding members of a Climate Club would themselves be large polluters, both in total emissions and in per capita terms, and therefore among those responsible for climate change. It would not be credible for these wealthy countries to adopt trade measures against low-income, low-emitting economies, while continuing to emit substantial amounts of GHG in absolute and per capita terms. In addition, potential supporters of a Climate Club are aiming to bring their CO<sub>2</sub> output down to a level which is already well above what 'laggard' countries would ever reach. From that point of view, the rest of the world might not be fully convinced that the intentions behind a Climate Club are exclusively based on climate considerations. Such a Club should not be perceived as a tool directed against weaker, less

developed non-members, but rather as a form of co-operation enabling faster, more widespread and efficient international action in the fight against climate change. It should supplement and not substitute existing processes which aim to counter the growth of average global temperatures.

### The EU as a Climate Club

Let's take the example of the EU. Current EU climate policy is *de facto* an incarnation of the idea of a Climate Club. It is composed of members sharing similarly ambitious climate policies and common internal instruments to reduce CO<sub>2</sub> emissions. The EU is the most ambitious signatory of the Paris Agreement, fully supporting global climate action. The EU has the most advanced system of GHG reduction based on the carbon market and the "cap and trade" mechanism. As the limit of permitted emissions decreases, demand for allowances pushes the cost of production to higher levels. In order to avoid affected industries relocating to countries with smaller or even no carbon costs, resulting in the so-called "carbon leakage", the European Commission proposed the [draft regulation of the Carbon Border Adjustment Mechanism, or CBAM](#). In a nutshell, CBAM seeks to apply obligations and costs to imported products, similar to requirements imposed on European production. That is why CBAM is the backbone of the EU's external climate policy. However, there are significant problems related to the effectiveness of the EU as a Climate Club. Even if this "European Climate Club" contains 27 members (plus those countries who are linked to the EU ETS), they are perceived as one entity and they contribute only a small portion of global emissions; around 8%.

At the moment, ambitions of unilateral EU action to introduce CBAM have met some prudent understanding as well as open opposition. Even if other countries have considered introducing carbon border adjustment, this has not yet materialised. The EU acting alone as a Climate Club risks provoking a negative reaction from even the EU's closest partners in climate negotiations, as there are some lingering concerns related to CBAM's compatibility with WTO trade rules. If and when they are affected, EU trade partners may look into any inconsistency between CBAM and trading rules to exercise pressure or take action which might lead to arbitration or dispute settlement procedures. This would negatively affect the cooperation needed within a larger Climate Club.

This also potentially weakens climate negotiations as the commitments made within UNFCCC would become less relevant.

### International Agreements

There is a substantial difference between CBAM's effects on international trade and its nature as an instrument fundamental to the Paris Agreement. Trade falls under the scrutiny of the WTO, based on well-established rules, advanced dispute settlement systems, and strong enforcement mechanisms, including permitted retaliation. The UNFCCC, which led to the creation of the Paris Agreement, is focused on mitigation measures preventing climate change, based on willingness and voluntary commitments. [The Article 3 p.5 on Principles of the UNFCCC](#) states 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". The Paris Agreement concentrates on emission within the sovereign territory of its members, whereas the WTO focuses on products moving between trading countries. In sum, the UNFCCC concentrates on the principle of origin whereas the WTO is based on destination principle.

The Paris Agreement is based on nationally determined contributions to the fight against climate change and it does not contain provisions directly affecting cross-border trade. [In the Doha declaration, WTO](#) members agreed to clarify the relationship between WTO rules and Multilateral Environment Agreements (MEAs), with respect to those MEAs which contain "specific trade obligations". Therefore, it does not yet create an immediate link between obligations under the Paris Agreement and WTO rules. Encouraging other parties of the Paris Agreement to embark on carbon pricing goes beyond its provisions. A Climate Club based on CBAM would *de facto* aim to ensure that other countries, including the least developed ones, should take up similar instruments like those adopted in the EU and put into effect more far-reaching policies compared to what they have voluntarily agreed within the UNFCCC.

There are also other environmental negotiations where the relationship between climate and trade was agreed upon. For example, in the outcome document of the United Nations Conference on Sustainable Development, entitled "[The future we want](#)", agreed with active involvement of the EU, the text of point 58 (h) urges countries to refrain from using unilateral economic, financial, or trade measures and also underlines that countries promoting green economy policies should avoid undertaking unilateral action to deal with environmental challenges outside the jurisdiction of the importing country. It has also been agreed that environmental measures addressing trans-boundary or global environmental problems, as far as possible, are to be based on international consensus. Also, in the earlier opportunity of the UN Rio de Janeiro Earth Summit in 1992, the Resolution adopted contained principles referring, among other things, to the issue of the use of trade policy measures. [The principle number 12](#) of its resolution repeats wording of the chapeau of Article XX of GATT, and continues by underlining two aspects, namely that unilateral actions to deal with environmental challenges outside the jurisdiction of the importing country should be avoided, and that global environmental problems should, as far as possible, be based on international consensus.

The Paris Agreement is not equipped with a system of sanctions or corrective measures in case of failure to comply with its provisions. That is not its only weakness, but this indisputably affects the potency of the negotiating leverage of the most ambitious members. All its signatories have agreed to periodically reconsider their own commitments, and that successive nationally determined contributions should represent a progression. However, there is no penalty for not making significant progress on declared policies, or even backsliding in real terms. It should be noted that for many less wealthy countries, this feature of the Paris Agreement was the only solution enabling them to accept the final text. It's possible that without such a bottom-up process of contributions to climate mitigation, there would be no agreement. It allowed many small, poor and unindustrialised countries to join the process.

### **The need to accelerate**

The acceleration of climate action requires a much stronger mechanism, which within the UNFCCC is not possible. We need a Climate Club of countries

who should feel responsible for the anthropogenic causes of climate change. Such a Club could be very useful, even if just a handful of large countries (considering the EU as one entity) are involved, but they should represent major economies/polluters. Just a few UNFCCC parties (EU+UK, US and China) represent [around half of global GHG emissions](#). But they do represent quite different approaches in their climate policies. They undertake different steps and represent different levels of ambition for climate action. The issue of comparability of effort and how this could be translated into the Club's functioning is crucial. But if [they were able to agree](#) on substance, i.e., the aims and modalities of the operation between themselves first, then the way to engage other polluters would be open. Therefore, the system of recognition and quantification of different climate action is the first challenge which must be addressed.

If the club were enlarged or measures of the club were to also be applied to India, Russia and Japan, it would represent an action that embodies about two thirds of global emissions. If the 10 following most emitting countries were also affected by the Club's measures, more than 80% of global emissions would be addressed. Without big emitters making decisive contributions to the global decarbonisation effort, the fight against climate change will not be successful. Big emitters bear crucial and indisputable responsibility. Club members should concentrate first on limiting the emissions of the group of large emitters and on carbon measures applied only to the most responsible countries. Club measures should not extend to the remaining 150+ countries who collectively contribute less than 20% to global emissions. Solutions must be found so that harsh measures are not applied to countries who hold only marginal responsibility for climate change.

The idea of a Climate Club should become less opaque and more outfitted. It cannot be achieved without creating adequate international legal reference. The informality of the Climate Club concept makes it politically attractive but practically difficult to put implement. A Climate Club must have a clear political mandate, a sufficient structure and modalities to develop itself, as well as instruments of delivery. There are many ways to enhance cooperation between Club members and many instruments that could be used. There are also a handful of practical issues to be solved as countries differ in their climate policies and measures. Many technical issues could

be clarified, including the fundamental issue of assessment of equivalence of regulatory and market measures. It must be based on rules which are clear for its members and understood by those who are not. It should provide facility of cooperation between those who belong and not be rigorous towards those who are responsible for climate change and do not belong. It should not be substituting or be in the opposition to the UNFCCC process, as the UN does provide foundations for embracing the global community in actions in this area.

### **Where should the Climate Club negotiations take place?**

There are a number of places where the discussion on a Climate Club could be promoted. The UNFCCC does not provide a proper framework, as a Climate Club is by essence of limited membership, and discussing it on the margins of COPs could result in the mistrust of others engaged within this forum.

The G7 or G20 certainly offers a framework where this idea could be given political importance. They are already engaged in the discussions aimed at accelerating climate action, and they are seen as potential backbone for [climate club or alliance](#). But both formations lack the legal and institutional instruments necessary to ensure implementation of actions of a Climate Club, such as border adjustment measures affecting other countries. And the recent attempt by the German Presidency of that forum have not sufficiently advanced this idea forward.

There have been very useful Major Economies Forum on Energy and Climate (MEF), established by the United States and bringing together the seventeen major greenhouse gas emitters. But similarly, it could not transform itself beyond a discussion club. The major problem is informality and the lack of implementing capacity.

There is also a proposal to make the OECD the hub for further development of this idea. The OECD has been successful with debating the taxation of multinational companies, based on the organisation decades-long experience of dealing with international finance, payments and tax issues. But if the Climate Club were to rely on Carbon Border Measures, it would essentially affect trade rules and trade flows.

Therefore, it is the WTO which could provide some legal and institutional anchoring for the Climate Club. The major complication for Climate Club actions

would be their compatibility with international trading rules. This controversy cannot be solved easily outside of the WTO. The advantage of this organisation lies with its indisputable expertise, experience with interpreting trade rules, and highly developed legal and institutional infrastructure, as well as the capacity to deal with the many technical problems involved. The WTO legal framework could help solve issues like labelling and documentation concerning production-related carbon emissions. The Agreement on Technical Barriers to Trade (TBT) could provide the proper base to clarify any problem in this area. Also, the issue of origin of products subject to carbon payments can be considered within the existing WTO rules.

Like no other, this organisation has at its disposal a quite efficient dispute settlement system, (even with – hopefully temporarily - not fully functional Appellate Body) which might appear necessary in the context of complicated obligations to differentiate between similar products obtained in low and high carbon emitting jurisdictions. There are also modalities within the WTO and wide experience of reaching agreements within smaller groups of its members. A Climate Club component negotiated within the WTO would also give new vigour to the trading system by helping to reconcile its rules with the climate measures. Most of these large emitting countries have signed a recent Ministerial Statement on Trade and Environmental Sustainability within ongoing [WTO discussions](#), where they have underlined their interest in progressing on trade and climate.

Converting the nebulous idea of the Climate Club into a tangible operational instrument is difficult but necessary. Determining its exact form, structure, rules and instruments will be in any case strenuous.

In verbal politics, many countries might share climate preoccupations and advocate for strong climate initiatives. However, linkages between political support and real commitments are not clear-cut. Even among like-minded, ambitious countries, there might be many differences how to move forward. But being serious about the Climate Club means it has to be formalised, including deciding that every constituent country is ready to undertake significant obligations.

The process of achieving such an agreement under any other umbrella will be difficult and lengthy, but without a more exact shape, the Climate Club will remain a loose idea without any real meaning. It might be difficult to convince everyone among the handful

of countries who contribute more than 1% to global GHG emissions to involve themselves in the negotiations. The group is diverse and beyond three indispensable participants, i.e., the EU+UK, US and China, the inclusion of some large polluters (such as Russia or Iran) might pose difficulties. But because all countries who are accountable for at least 1% of GHG emissions evidently have an elevated responsibility, they should therefore be covered by Climate Club actions.

### Future Recommendations

The way forward should address three fundamental issues of the Climate Club. Firstly, it should be linked to well-developed legal and institutional framework enabling anchoring any instrument used by the Club members. Secondly, it should deal with the comparability of the level of ambition by solving the question of assessment of efficiency of different approaches and instruments. Thirdly, it should find a way to address problems created by big emitters and eliminate the risk of its perception as a tool to force small, poor countries to undertake efforts beyond their capacity.

1. Therefore, the first step is for the EU and the US, who are the most likeminded partners, to work on the details of the idea. At this stage, some other countries could also be approached like Canada, Japan, Australia, and New Zealand to name just a few, but American participation is decisive for the progress on the issue of comparability of effort.
2. The presence of the US is also crucial if China is expected to be rapidly involved. There are many similar threads of transatlantic cooperation of the EU and the US which would enable progress in debates on those aspects of climate, where differences are still important. If the EU and US could reach a common understanding, it would be easier to bring China to the negotiating table.
3. Only after the EU and the US reaching an agreement on the modalities of the Climate Club might all the other important participants seriously consider their involvement. The Club can be based on Carbon Border Adjustments and other instruments of international climate actions, but it will require a common understanding on how they are applied. The Club should start with developing standards and details of implementation of carbon border adjustments, solving many complicated technical issues such as the methods of calculation of carbon emissions levels in traded products, equivalence of other measures, rules of carbon origin, etc.
4. In parallel, initiators of the Club should bring the discussion to WTO in order to anchor actions in its legal framework. It could even lead to an agreement, between a limited number of WTO members, a sort of Plurilateral Agreement on Carbon Border Measures. To make it clear that Climate Club actions are permitted to target only large and significant emitters, a type of WTO Climate Waiver could be negotiated.
5. The Climate Club should respect that all other, smaller, less industrialised countries, being negligible emitters of GHG (well below 1% of global emissions) are not subject to measures taken by Climate Club members. More developed but small economies could be expected to join the Climate Club, even if their contribution to global emissions is not significant in absolute terms. As far as all other countries are concerned, the approach should be different. They should be helped to deliver what they promised under the Paris Agreement and not threatened by applying coercive instruments of Climate Club members, under the condition that they do not increase their emissions due to carbon leakage.

6. In order to ensure effective action in the long run, the Club should make it clear that any country which goes beyond the 1% threshold of global GHG emissions, thus becoming decisively responsible for climate change, should be subject to the disciplines, rules and instruments of the Climate Club. This would help enlarge the Club and its instruments to anyone else after its operations are proven to be clearly effective in their impact on the de-carbonisation of the largest emitters.

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