

# Carbon Border Adjustment Mechanism (CBAM)

- What is it about? When will it come into force?

April 2023

# EU Climate Policy

Brief scene setter

# EU Aims at Climate Neutrality

## How to do it?

- **EU Emissions Trading Scheme (ETS)**

- Introduced in 2005 and developed stepwise over the years
- Cornerstone of the EU's policy to combat climate change – approx. 40% of EU GHG emissions
- Covers large industrial and electricity plants
- Carbon leakage addressed via free allocation of emission allowances

- **Sectors outside EU ETS**

- Buildings, transport, small industries, agriculture – approx. 60% of EU GHG emissions
- Member States national measures
- 8 Member States (e.g. Sweden) have national carbon taxes

- **EU climate goals, decided in 2019**

- Political ambition is a legal obligation for the EU (EU Climate Law)
  - First climate-neutral continent in 2050
  - Reduce carbon emissions by 55% in 2030

- **EU Green Deal, presented in 2019**

- Fit for 55 Package legislative proposals in 2021, such as
  - Review of the EU ETS – tightened, extended to other sectors
  - Free allocation is phased out
  - Prevent carbon leakage to ensure effectiveness of EU climate policy = CBAM is introduced

- **CBAM is an essential part of EU Climate Policy, not a protectionist measure.**

# CBAM

## Global context

# Why is There a Need for CBAM?

- Global climate challenge requires urgent action – time for action is now!
- Paris Agreement; recent IPCC report
- EU raises its climate ambition
- Differences in climate ambition among EU's trading partners => CBAM prevents carbon leakage to ensure effectiveness of EU climate policy on the EU market
- Incentivise ....
  - 3<sup>rd</sup> country producers to reduce emissions
  - 3<sup>rd</sup> countries to adopt green policy frameworks



# CBAM or International Coordination?

- CBAM has a strict climate objective
- CBAM favours decarbonisation efforts in third countries
  - Deduction of explicit carbon price paid in 3<sup>rd</sup> countries from CBAM obligation
  - Actual emissions methodology
  - Countries linked to EU ETS will be excluded
  - Possible international agreements on how to take account of carbon price
- CBAM does not preclude continued joint work on international coordination of carbon pricing

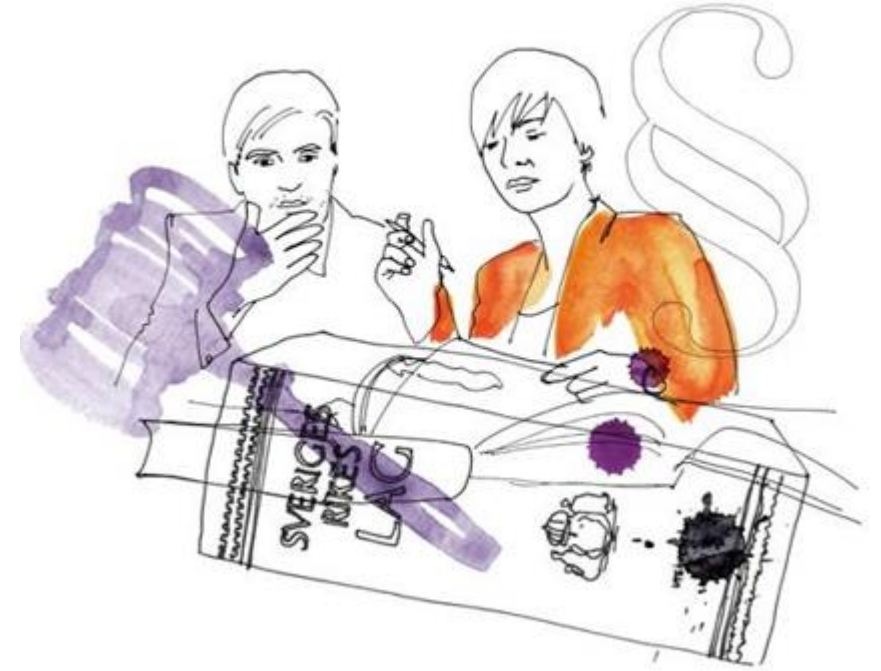


# CBAM

## EU legal adoption process

# When Will We Know All the Details? I

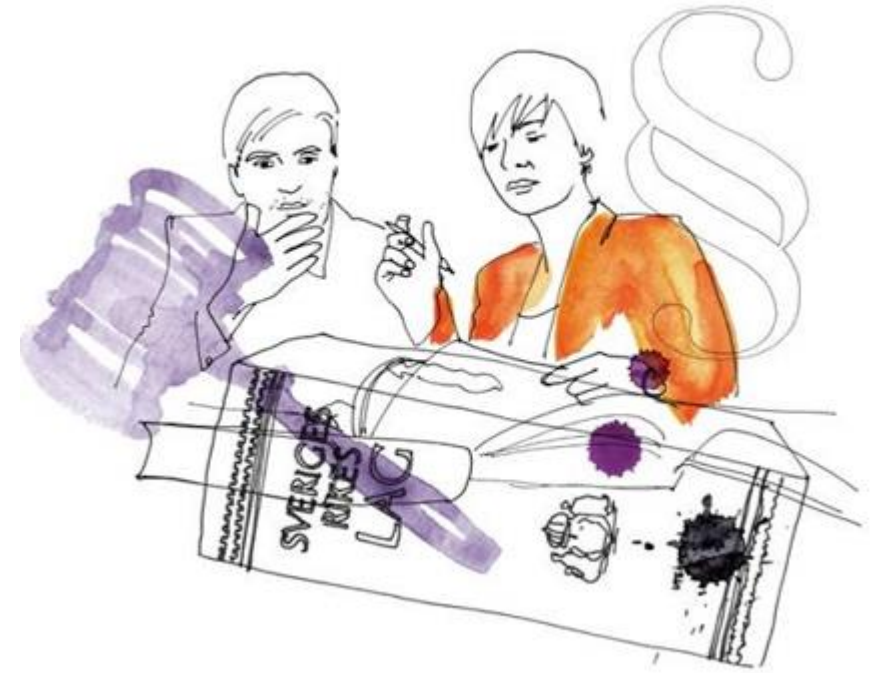
- **CBAM Regulation** – major framework
  - December Political agreement between EU co-legislators  
(<https://data.consilium.europa.eu/doc/document/ST-16060-2022-INIT/en/pdf>)
  - Spring 2023 Formal adoption by EU co-legislators
    - 19 April European Parliament vote
    - 25 April EU Council vote
    - 10 May Formal signing ceremony by co-legislators
  - 1 October 2023: Transitional period starts - reporting
  - 1 January 2026 : Definitive period starts – financial obligation; EU imports only by authorized CBAM declarants





# When Will We Know All the Details? II

- **Secondary legislation** – supplement framework
  - Adopted by EU Commission based on empowerments in CBAM Regulation, prepared by CBAM Committee (Member States Representatives) and stakeholder views
  - 12 *implementing acts*, to ensure detailed uniform application
    - One on methods for reporting during transitional period; as soon as possible (summer 2023);
    - 11 others (sufficiently prior to 1 January 2026)
  - 4 *delegated acts* – reflect certain developments
    - E.g. circumvention, adding countries to list of countries excluded from CBAM fulfilling certain criteria, such as linking to EU ETS



# CBAM

## Challenges when designing CBAM

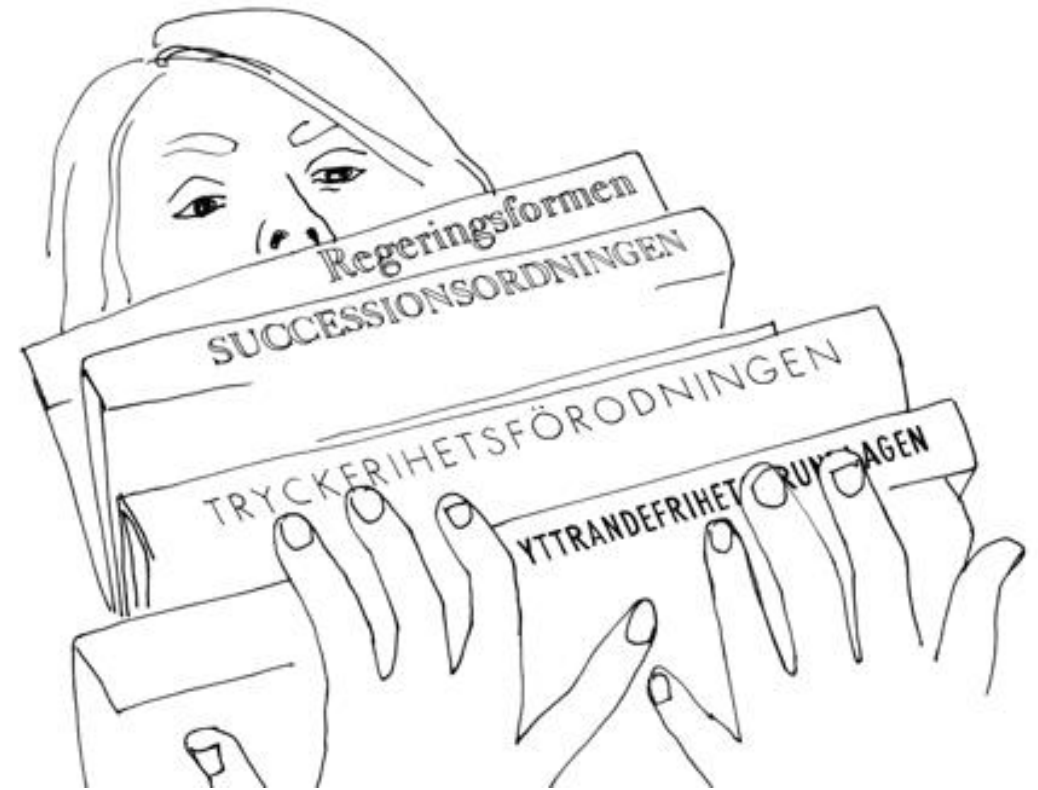
# Specific considerations during EU deliberations.....

- Which sectors and which specific goods?
- Direct emissions as well as indirect emissions?
- Calculation method of actual emissions in line with EU ETS
  - EU ETS installations vs CBAM goods
  - WTO conformity
- Trajectory for phasing in of CBAM and phasing out of free allowances under the EU ETS
- Export carbon leakage
- Governance model



# CBAM Regulation – changes between EU Commission July 2021 proposal and Final Agreement between EU co-legislators)

- Major changes:
  - Delay of *entry into force* to 1 October 2023.
  - Some additional *goods* added to CBAM scope
  - *Indirect emissions* in some goods added to financial CBAM obligation
  - Some changes of *pace of phase in* of CBAM obligation
  - Extended *review clauses*
  - *Small consignments* of goods excluded (150 €)
  - *Governance* – more centralised tasks at EU Commission, less on national EU authorities



# CBAM

## A closer look at the design

# CBAM Design

## Key Elements

- Addressed to companies, not countries
  - Based on actual verified carbon emissions embedded in imported goods
  - Focus on goods in carbon intensive sectors
- A Regulation mirroring EU ETS carbon pricing to the extent possible
  - Obligations on EU importers
  - Not a tax; not a customs duty
- Climate objective
- Compliant with WTO and in line with international trade rules



Photo: Maskot / Folio



# Goods in CBAM Scope

## General Basics

- Selected on basis of three criteria
  - High risk of carbon leakage (high carbon emissions; high level of trade)
  - Covering major part of carbon emissions under EU ETS
  - Practical feasibility to calculate embedded emissions in goods
- First phase
  - Goods within limited number of sectors
  - Goods defined by CN codes
- Further stages, following review post 2025
  - Extending to other sectors under EU ETS



Photo: Folio Images

# Goods in CBAM Scope

## Specific (Final Agreement)

- Goods in the following sectors:
  - Iron & Steel, incl. some precursors
  - Aluminium
  - Cement
  - Fertilisers
  - Electricity
  - Hydrogen
- Direct and indirect emissions:
  - Transitional period 2023-2025, reporting on actual direct as well as indirect emissions
  - Final period from 2026, declaring
    - Electricity: By default values, possibility to show actual verified direct emissions
    - For other goods, two groups of goods:
      - Group 1: Actual verified *direct* emissions; alt. use of default values (incl. mark-ups)
      - Group 2: Group 1 + indirect emissions (default values)



Photo: Lars Thulin / Johnér



# Carbon Price, from 1 January 2026

- Equal carbon pricing
  - EU companies pay a carbon price via EU ETS on goods produced in the EU
  - Importers pay a carbon price, corresponding to the EU ETS price
  - The CBAM obligation only applies if EU ETS free allowances has been phased out
  - Gradual phase in of CBAM obligation
    - Mirroring the phase out of EU ETS free allowances
    - COM proposal: 2026-2035 Linear 10% annual phase in
    - Political agreement dec 2022: 2026-2034, but slower pace from start
- No double pricing
  - An explicit carbon price paid in a 3<sup>rd</sup> country for the embedded emissions in imported goods will be deducted from the CBAM obligation



# How is Carbon Price Paid in 3<sup>rd</sup> Country Determined?

- Explicit carbon price (*Art. 3 (23) of CBAM Regulation*)
  - *'monetary amount paid in a third country, under a carbon emissions reduction scheme, either in the form of a tax, levy, fee or emission allowances under a greenhouse gas emissions trading system, calculated on greenhouse gases covered by such a measure, and released during the production of goods'*
- In line with WTO rules, mirrors EU carbon pricing



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# CBAM

## CBAM obligations on EU importers from 1 October 2023 vs from 1 January 2026

# What Happens During the Transitional Period?

(1 October 2023 – 31 December 2025)

- The Customs Declarant (the importer) reports embedded direct and indirect emissions
  - CBAM goods imported to the EU from 1 October 2023
  - Report by each quarter; first report by 31 January 2024
  - No verification of emissions
  - *'Effective, proportionate and dissuasive'* penalty by national CBAM Authority on importer if not complying
  - Methodology and criteria for penalty forthcoming in implementing act
  - Reports submitted to EU Commission
    - To gather data for forthcoming implementing acts for definitive period
    - 'Learning by doing' period for business



Photo: Folio Images

# Obligations on Importers in Definitive Period I

## (from 1 January 2026)

- Goods can only be imported to the EU by an authorised CBAM declarant
  - Importer has to be established in an EU Member State
  - Authorisation by the CBAM Authority in the Member State of establishment, demonstrating financial and operational capacity
  - Application possible from 31 December 2024
- Yearly declaration of CBAM imports during previous calendar year
  - By 31 May 2027 submit CBAM declaration for imports during 2026
    - Specifying embedded emissions according to laid down methodology,
    - Ensuring that declared emissions are verified by an accredited verifier and include relevant verification reports
    - Calculating CBAM certificates to be surrendered
  - By 31 May surrender CBAM certificates covering declared emissions
  - Reviews of declarations by EU Commission and CBAM Authorities; non-compliance results in penalties



Photo: Thyra Brandt / Folio



# Obligations on Importers in Definitive Period II

(from 1 January 2026)

- Purchase of CBAM certificates
  - 1 CBAM certificate equals 1 ton of embedded emissions in goods
  - Authorised CBAM declarants buy at common EU auction platform
  - Price = average weekly price of EU ETS allowances
  - Upon purchase, CBAM certificates are registered in account of authorised CBAM declarant in CBAM Registry
  - No trading allowed between authorised CBAM declarants
  - An authorised CBAM declarant must ensure CBAM certificates for 80% of embedded emissions in his account by end of each quarter
    - Non-compliance may lead to revoking status of authorised CBAM declarant
  - Limited possibility to re-sell surplus CBAM certificates to the EU COM.
- Ensure that an accredited verifier will verify the embedded emissions
  - Use person accredited as EU ETS verifier, or
  - A person may seek authorisation by an EU Accreditation Body as an CBAM verifier.

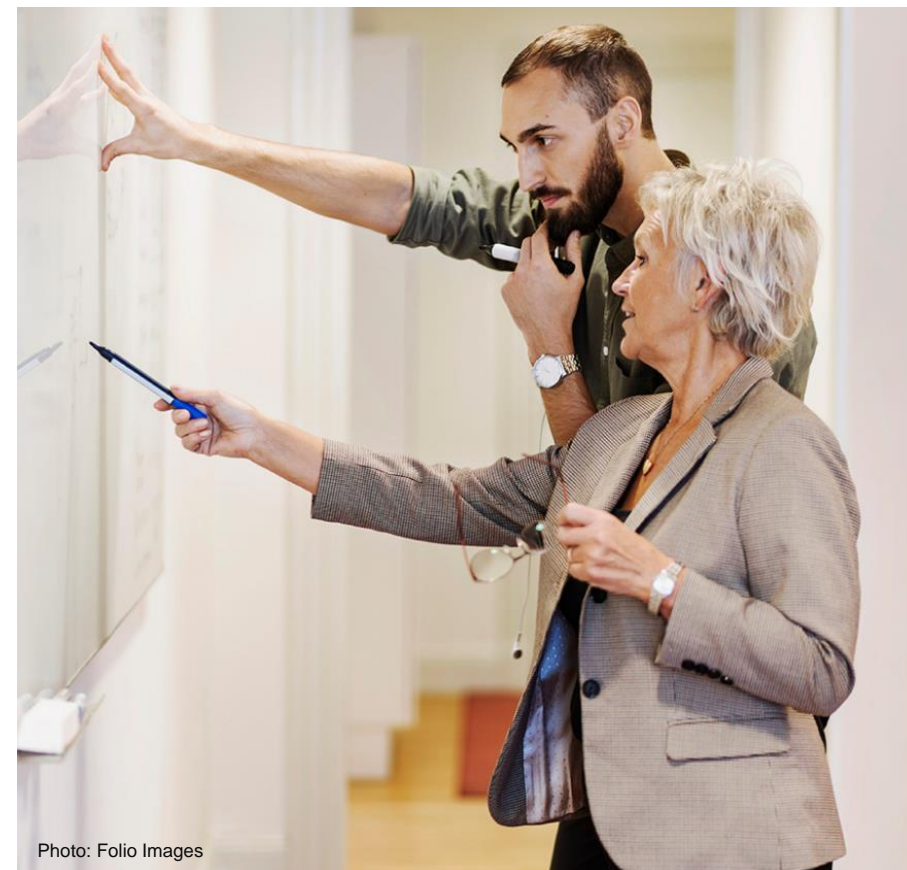


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# Role of a 3<sup>rd</sup> Country Producers

- All legal CBAM obligations on the EU importer, not on 3<sup>rd</sup> country producer, but ....
  - The EU importer is obliged to give detailed info on embedded emissions in the imported goods =>
  - Methods ensuring that access to data from the 3<sup>rd</sup> country producers ought to be part of negotiated trade deals on imports from 1 October 2023; from 1 January 2026 these data needs to be verified by an accredited verifier.
- A 3<sup>rd</sup> country producer may register contact information and activity in EU CBAM Registry
  - To facilitate contacts between importers and 3<sup>rd</sup> country producers; possible already from 1 Oct. 2023
  - The 3<sup>rd</sup> country producer shall ensure verification of embedded emissions.

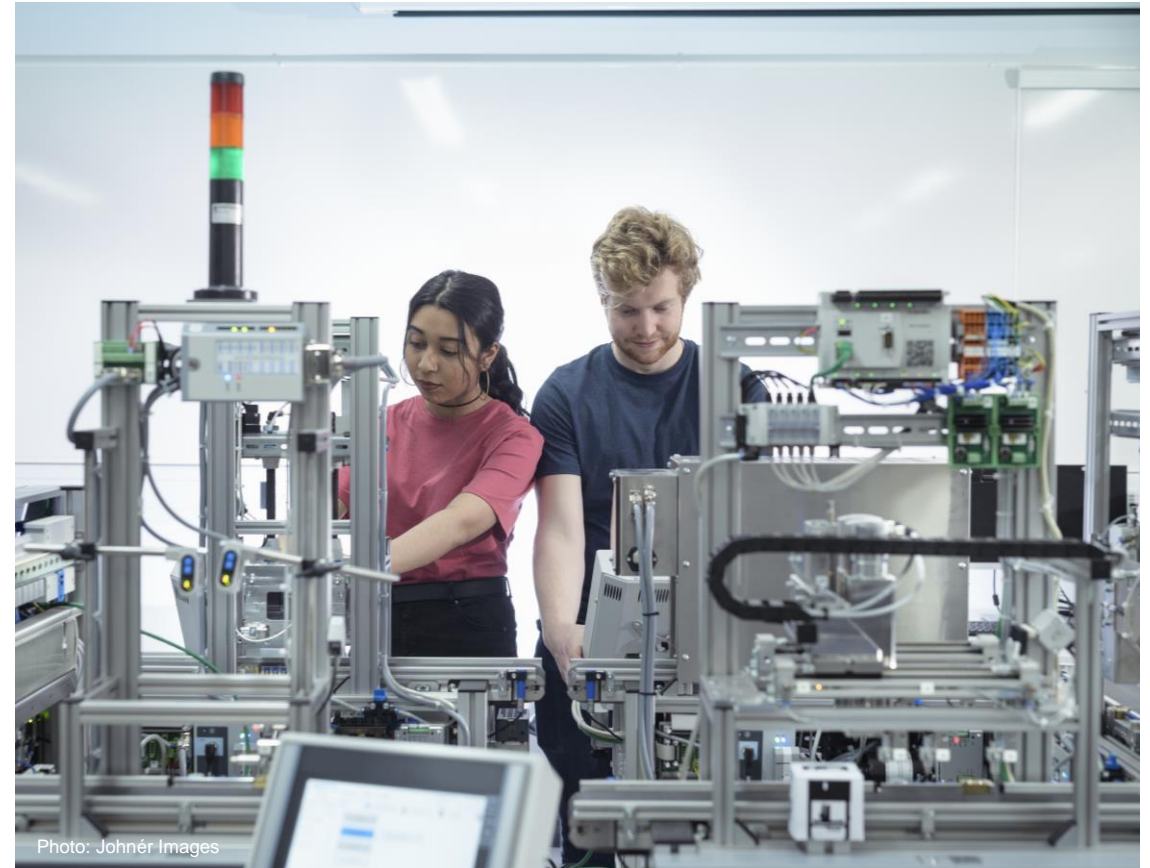


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# CBAM – Questions?

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