

REGULATORY | FEBRUARY 2023

## CBAM: CAN THE EU ACHIEVE CARBON ADJUSTMENT BEYOND ITS BORDERS?

The EU's carbon border adjustment mechanism ("CBAM"), part of the bloc's "Fit for 55" package aimed at cutting emissions by 55% by 2030, will take effect from 1 October 2023. Importers of cement, iron, steel, aluminium, fertilisers, hydrogen and power will have to report on volumes of imports and corresponding emissions from that date, with payment obligations coming into effect in 2026.

### Achieving consensus within the borders

After years of discussion, it was only in December 2022 that the European Commission, the Council of the EU and the European Parliament agreed on the terms of the CBAM Regulation. One of the last minute changes was the inclusion of energy production emissions within the scope of the tax, at the behest of the European Parliament.

The tax on emissions released during the production of affected goods will be at a rate equivalent to the price which would have been paid in the EU Emissions Trading System (EU ETS), if the emissions had taken place in the EU. There will however be a reduction where the importer can demonstrate that a similar tax has been paid in the place of production.

The CBAM will be phased in and the free allowances currently available to EU installations in the same industries will be phased out between 2026 and 2034.

### Which emissions are targeted?

The list of products caught by the CBAM Regulation focuses on the early stages of the value chain. A wide range of goods with a smaller element of the target products is excluded. It is hoped that the impact on small businesses and consumers will be thereby reduced.

However, the companies whose emissions are caught are likely to be larger ones: those most able to move elements of production outside the EU, importing finished goods not caught by the new tax, or directing towards the EU those items with greener production processes and sending dirtier items elsewhere.

### Your products, your carbon and your borders

Whether the CBAM is successful in motivating affected industries to engage in green innovation and foreign governments to impose green taxes remains to be seen. What is clear though is that the CBAM is coming.

In order to be ready for the changes it will bring, if you are in one of the affected sectors and your products are destined for Europe, you will need to:

- identify the types, volumes and *embedded emissions* of products caught
- establish your *designated authority* within the EU for reporting purposes and the *authorised importer* required to comply with CBAM obligations
- monitor and budget for CBAM costs
- work with your supply chain to measure and record emissions and taxes paid on them
- update contracts to ensure the availability of data you need and allocate cost

Whether or not you are affected now, you will need to monitor planned extensions to the CBAM programme in the future and the development of similar initiatives in other parts of the world.

For more information, please contact the author(s) of this alert



**DIANA FRANCE**

Partner, London

**T** +44 (0)20 7264 8103

**E** [diana.france@hfw.com](mailto:diana.france@hfw.com)

**[hfw.com](https://www.hfw.com)**

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