

European Commission releases proposal for a Carbon Border Adjustment Mechanism

Indirect Tax Alert | Global Trade

July 27th 2021

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On July 14th 2021 the European Commission adopted its proposal to establish a Carbon Border Adjustment Mechanism ('CBAM'). The CBAM is to prevent carbon leakage¹ by charging a carbon price on certain goods imported into the European Union ('EU').

Detailed discussion

On July 14th 2021 the European Commission published the so-called 'Fit for 55 Package', that includes several proposals to transform the EU's economy and society to meet climate ambitions.² The proposal to establish a CBAM was announced in the European Commission's Covid-19 recovery plan of May 27th 2020, but is now published in full detail as part of this package.³

The CBAM is a climate measure that extends the current EU Emission Trading System ('EU ETS') to imported goods and creates a level playing field by ensuring equivalent carbon pricing for imports and domestic products. The CBAM Regulation provides for a phased introduction of the CBAM by way of a transitional period from January 1st 2023 until December 31st 2025. As of January 1st 2026 the CBAM comes into force in full.

During the transitional period only quarterly reporting obligations are required by customs declarants for imports of goods listed in Annex I of the CBAM Regulation (see below). After the transitional period, a carbon price will be levied

on the importation of these goods by means of CBAM certificates in addition to the reporting obligations.

Which imports need to be reported under the CBAM Regulation?

Imports that need to be reported are:

- Imports of goods listed in Annex I of the CBAM Regulation into the EU;
- Imports of processed goods into the EU resulting from the Inward Processing Procedure ('IPR') if the goods placed under IPR are listed in Annex I (even if the processed goods are not listed in Annex I);
- Imports of goods processed under the Outward Processing Procedure into the EU if the processed goods are listed in Annex I (not during the transitional period);
- Imports of goods listed in Annex I imported into the EU under the returned goods relief (not during the transitional period).

The information to be included in the annual CBAM declarations by authorized declarants upon 2026 per type of goods imported during a calendar year is i) the total quantity, ii) the embedded emissions, iii) the total number of CBAM certificates corresponding to the total embedded emissions and iv) carbon costs paid in the country of origin. During the transitional period the quarterly reports to be submitted by the customs declarant follow the same scope,

¹ In this context, carbon leakage is the risk that companies based in the EU could move carbon-intensive production abroad to take advantage of lax standards, or EU products could be replaced by more carbon-intensive imported products.

² See EY Global Tax Alert, [European Commission proposes legislative package including](#)

[environmental tax measures to support EU climate ambitions](#), dated 15 July 2021.

³ See EY Global Tax Alert, [European Commission publishes proposal for recovery plan and adjusts 2020 Work Programme](#), dated 28 May 2020.

except for the reconciliation of CBAM certificates which do not yet exist in the transitional period.

What products will be subject to CBAM?

Annex I of the current proposal lists the CN-codes⁴ of the products that will be subject to a carbon price at import (list of CN-codes is included in the Appendix of this alert). In summary, the list is now limited to cement, iron & steel, aluminum, fertilizer and electricity as for these products there is, according to the European Commission, a high risk of carbon leakage. During the transitional period the European Commission may decide to extent the scope so that it also covers other products and/or indirect emissions⁵. This decision will be made based on continuous research about the effect of bringing these additional products under the scope of the CBAM Regulation and how to properly calculate the emission footprint of imported products. The imports of these products can only be made by an 'authorized declarant' (see below).



Who is an authorized declarant?

A declarant is a person lodging a customs declaration for release for free circulation in its own name or the person in whose name such a declaration is lodged. The declarant is required to be established in the European Union. The 'authorized declarant' status is granted by the competent (CBAM) authorities. Such authorization is only granted if this person requesting for the authorization complies with certain (compliance) conditions.

Under the CBAM Regulation, the authorized declarant status is important, considering that only an authorized person is entitled to:

- Import goods listed in Annex I of the CBAM Regulation;
- File CBAM declarations;
- Purchase CBAM certificates.

The information on the embedded emissions in the imported goods will be available to the authorized declarant if he (or a related party) is also the operator or installation producing the imported goods. In other cases, the authorized declarant must obtain the information from a registered operator or installation in a third country. Certain information can be made available from a central database in case of registered operators or installations.

Who is a registered operator or installation?

An operator or installation in a third country (i.e., a non-EU Member State) may request the competent (CBAM) authorities to register in a centralized database. Once registered, the operator or installation can disclose information on the embedded emissions to authorized declarants. Once registered the operator or installation should comply with several reporting obligations.

What is a CBAM certificate?

For importing goods listed in Annex I of the CBAM Regulation, the authorized declarant needs to purchase CBAM certificates from the competent (CBAM) authorities in the country where the declarant has been authorized. The CBAM certificates should correspond to the total embedded emissions in the imported goods listed in Annex I of the CBAM Regulation. The CBAM certificates are surrendered to the competent

⁴ 'Combined Nomenclature' is a EU's tool for classifying goods for imports/exports from/to the EU and trade between EU Member States. See further detail on the covered goods in the Appendix of this alert.

⁵ 'Indirect emissions' mean emissions from the production of electricity, heating and cooling, which is consumed during the production processes of goods.

authorities by means of the annual CBAM declaration by May 31st of each year for the calendar year preceding the surrender.

The price of a CBAM certificate is equal to the average price of the closing prices of EU ETS allowances on the common auction platform in accordance with the procedures laid down in the EU ETS Regulation for each calendar week.

How to calculate the embedded emissions?

The embedded emissions in goods listed in Annex I are calculated in accordance with the formulas in Annex III of the CBAM Regulation. The emissions declared in the CBAM declaration need to be verified by a verifier accredited in accordance with the provisions in the CBAM Regulation.

Are there any exemptions provided for under the CBAM Regulation?

Yes. Some countries of origin are exempt from CBAM altogether (see below). Next to that, under certain conditions the carbon price paid in the country of origin of the goods listed in Annex I can lead to a reduction in the number of Carbon certificates that needs to be submitted. The documentation supporting the carbon price paid in a country of origin needs to be certified by an independent person. Also, a reduction of CBAM certificates to be submitted will be available to import of goods for which the EU still allocates free certificates through the EU ETS to EU established installations and operators.

Is the country of origin of the goods important?

Yes. The CBAM Regulation does not apply to goods originating in one of the following countries/territories: Iceland, Liechtenstein, Norway, Switzerland, Büsingen, Heligoland, Livigno, Ceuta or Melilla. Therefore determining the country of origin in accordance with the customs rules remains very important.

Who are the competent CBAM authorities?

EU Member States shall designate the competent CBAM authority to carry out the obligations under the CBAM Regulation. The competent authorities will be listed in an official publication of the European Commission.

Actions for business

Businesses are recommended to:

- Assess potential impact of compliance and reporting obligations arising from the CBAM Regulation (and the concurrent changes to the EU ETS) to their businesses.
- Assess the financial impact of CBAM based on the current supply chain and take appropriate actions to mitigate the financial impact by rethinking e.g. the structure of the supply chain, sourcing strategy, production planning and technical improvements to reduce embedded emissions in imported products.
- Calculate the emissions embedded in goods imported into the European Union subject to the CBAM Regulation, either or not together with manufacturers.
- Arrange for timely registrations of third country operators and installations.
- Rethink the future EU importation set-up, taking into account customs, CBAM and information confidentiality considerations.
- Determine the technical facilities of measuring accurate weights (especially for bulk products).
- Determine the CN-codes and country of origin of the goods imported into the EU to determine whether they fall under the scope of the CBAM Regulation.

Appendix

Current list of goods covered by CBAM according to the classification of these goods in the Combined Nomenclature (abbreviated, further specifications apply):

<i>Cement</i> 2523 10 00, 2523 21, 2523 29 00, 2523 90 00	<i>Iron and Steel</i> 72 (except 7202 and 7204), 7301, 7302, 7303 00, 7304, 7305, 7306, 7307, 7308 (excluding prefabricated buildings of heading 9406), 7309, 7310, 7311
<i>Electricity</i> 2716 00 00	
<i>Fertilizers</i> 2808 00 00, 2814, 2834 21 00, 3102, 3105 (except 3105 60 00)	<i>Aluminum</i> 7601, 7603, 7604, 7605, 7606, 7607, 7608, 7609 00 00

The above is based on our interpretation of current tax legislation and case law published to date. This Indirect Tax Alert provides general information with no pretension of completeness, and it is not a tax advice.

Information

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