

CBAM Series

As part of the Carbon Neutrality Action Initiative and to mark the one-year anniversary of the Chamber's report [Carbon Neutrality: The Role of European Business in China's Race to 2060](#), we will publish a series of posts on the EU's Carbon Border Adjustment Mechanism (CBAM).

Recent Developments:

On 10th May 2023, the European Parliament and the European Council, as co-legislators, signed the final Carbon Border Adjustment Mechanism (CBAM) Regulation. **The regulation officially entered into force on 17th May 2023**, the day after its publication in the Official Journal of the EU.

On 13th June 2023, the European Commission published a first [call for feedback on the rules governing the implementation of the CBAM during its transitional phase](#), which starts on 1st October 2023 and runs until the end of 2025.

On 17th August 2023, the European Commission adopted the rules governing the implementation of the Carbon Border Adjustment Mechanism (CBAM) during its transitional phase, which starts on 1st October 2023 and runs until the end of 2025.

The [Implementing Regulation](#) details the transitional reporting obligations for European Union (EU) importers of CBAM goods, as well as the transitional methodology for calculating embedded emissions released during the production process of CBAM goods.

To help both importers and third country producers, the Commission also published [guidance](#) for EU importers and non-EU installations¹ on the practical implementation of the new rules. At the same time, dedicated information technology (IT) tools to help importers perform and report these calculations are currently being developed, as well as training materials, webinars and tutorials to support businesses when the transitional mechanism begins.

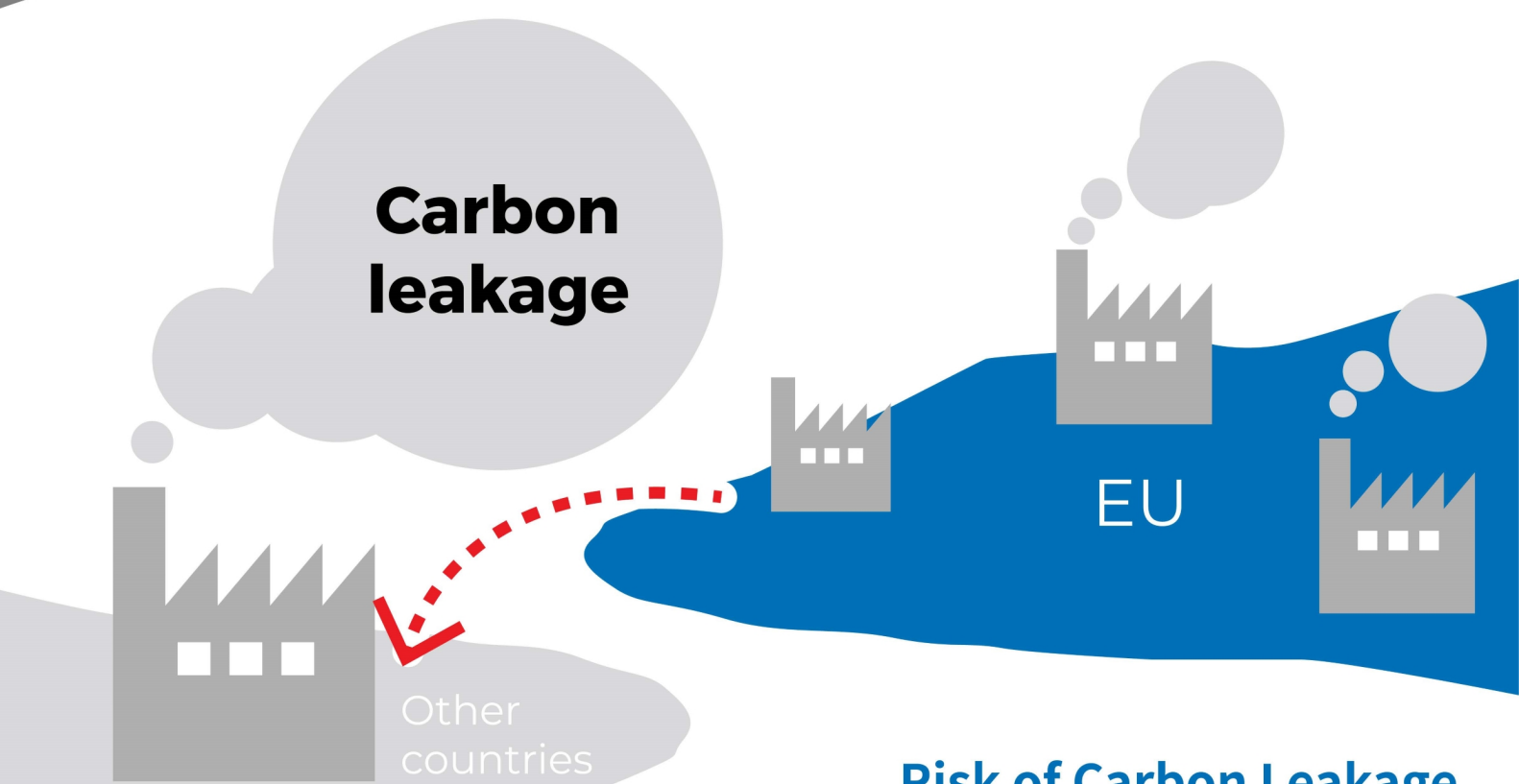
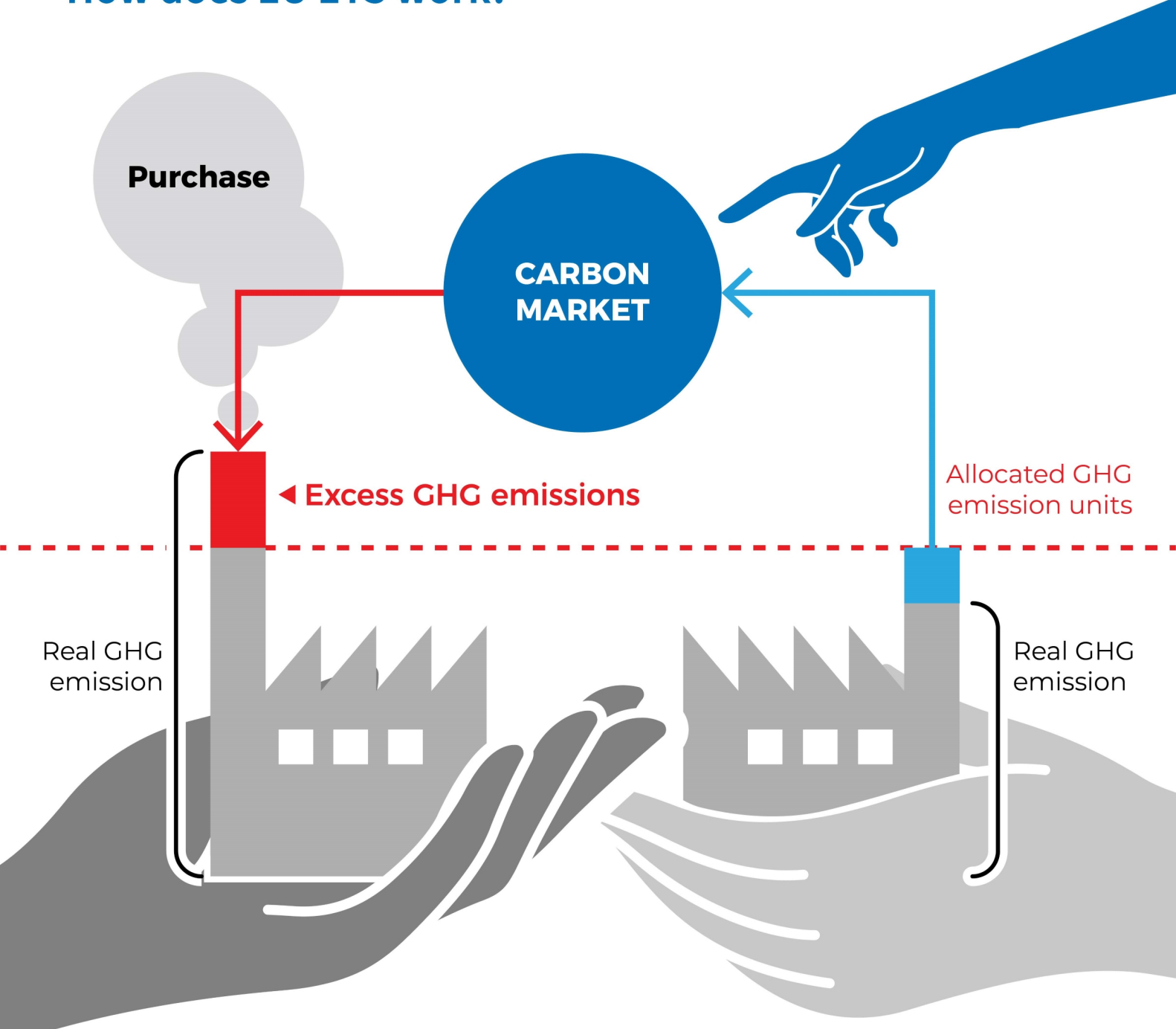
¹ An 'installation' means a stationary technical unit where a production process is carried out.

Carbon Border Adjustment Mechanism (CBAM) Series

What is the EU Emission Trading System (ETS)?

‘Cap and trade’: Greenhouse gas (GHG) emissions over the permitted limit (the cap) can be traded as a commodity on the EU carbon market.

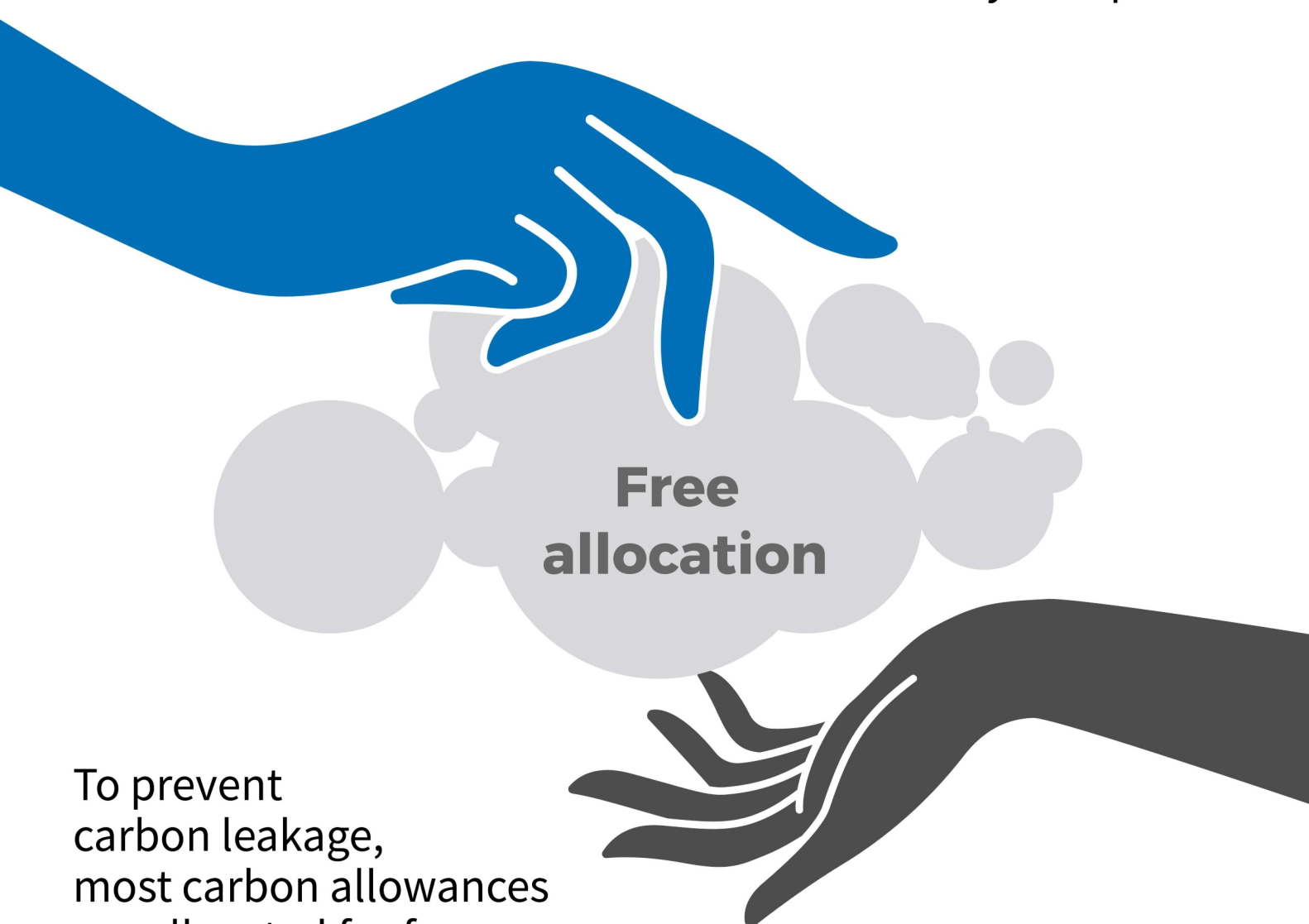
How does EU ETS work?



Risk of Carbon Leakage

‘Carbon leakage’ occurs when companies move from the EU to countries with lower environmental standards to avoid the costs associated with the EU ETS.

→ This means global emissions do not decrease overall; and the competitiveness of EU industry is impacted.



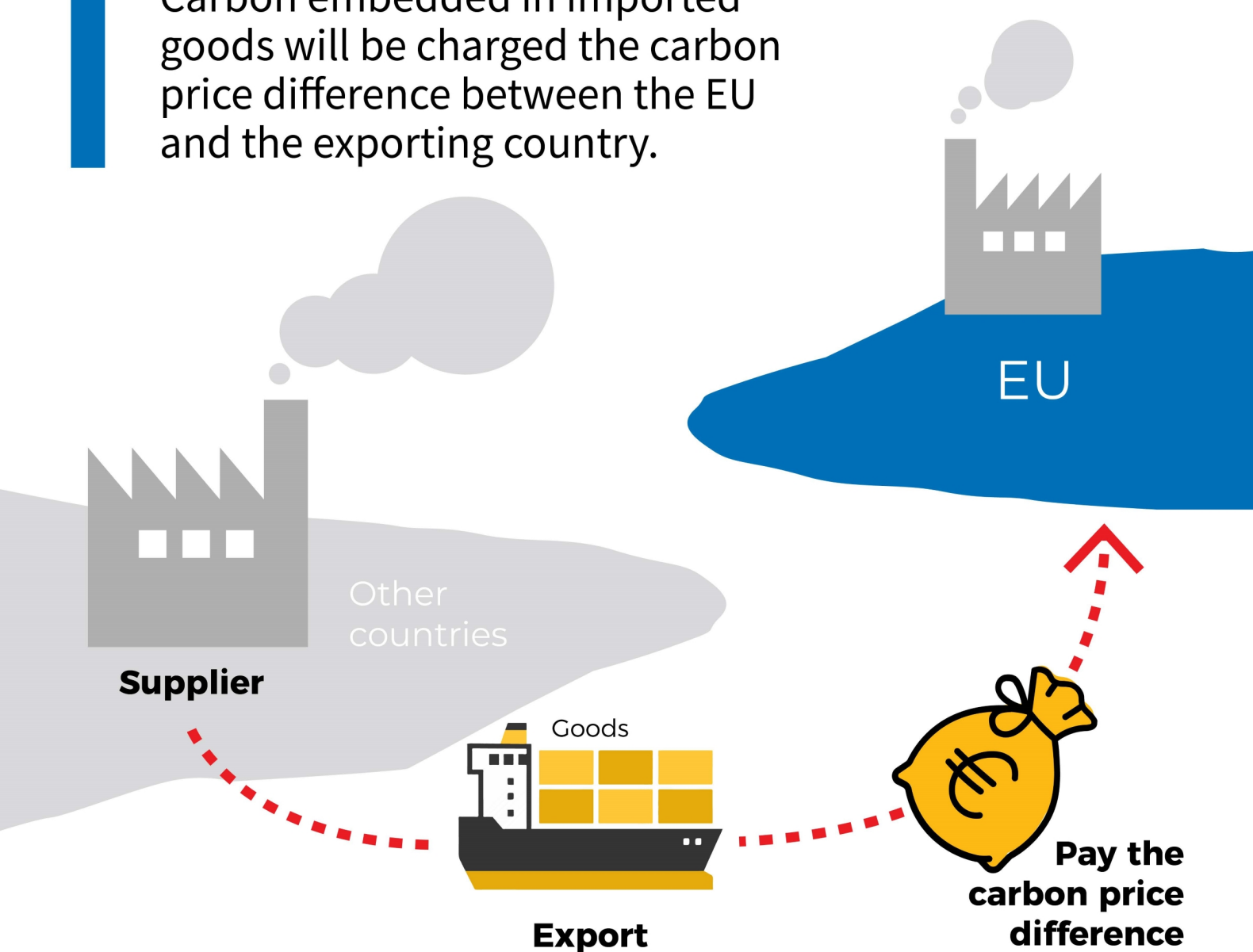
To prevent carbon leakage, most carbon allowances are allocated for free.

→ However, free allocation in the long-term undermines the ‘polluter pays’ principle and risks slowing down the EU’s decarbonisation efforts (lack of incentives to cut emissions).

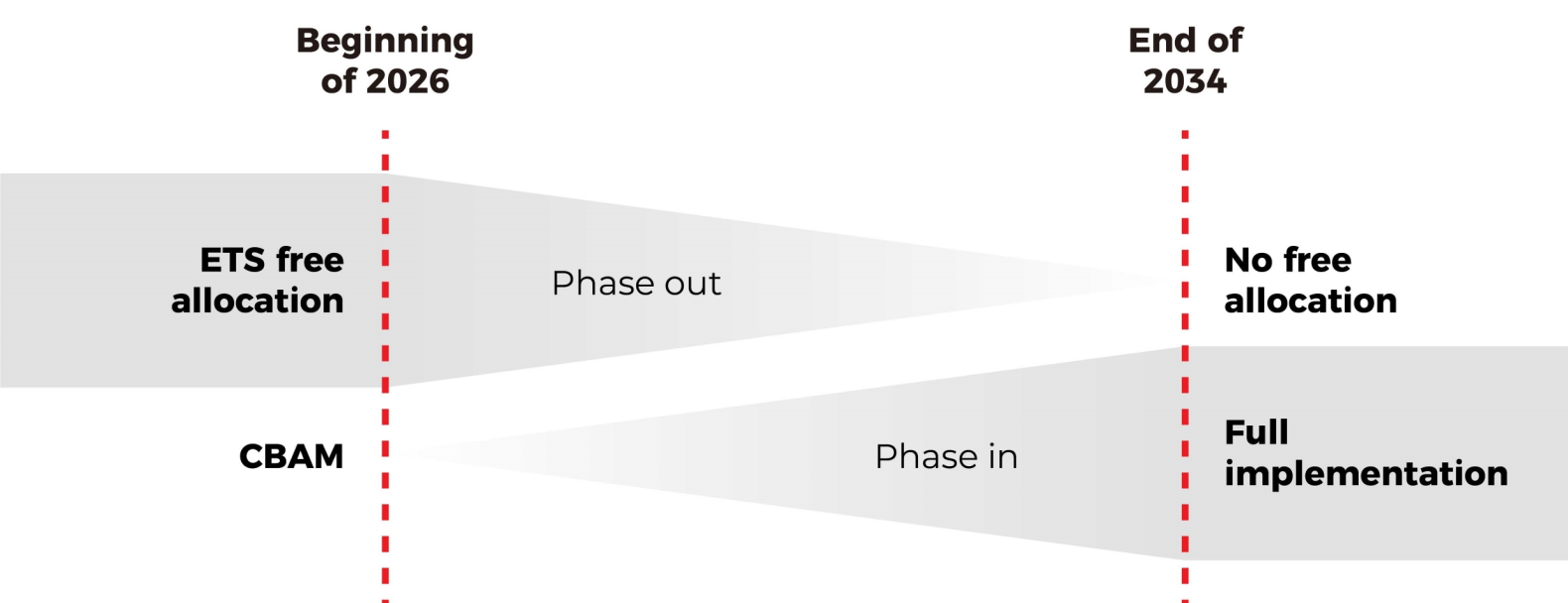
Carbon Border Adjustment Mechanism (CBAM)

The CBAM will make the EU ETS more effective and counter carbon leakage, while incentivising third countries to reduce emissions:

Carbon embedded in imported goods will be charged the carbon price difference between the EU and the exporting country.



Countries that apply the EU ETS or that are linked to it will be excluded from the CBAM.



While the CBAM is phased in, free allocation of allowances under the EU ETS will be gradually phased out over a nine-year period (from 2026 to 2034).

Roadmap

Transition period
(**1st October 2023–
31st December 2025**):
quarterly reporting is
mandatory.

Post-transition period:
From **1st January 2026**,
payments will be
mandatory.

Full implementation:
2035, when free EU
ETS allowances will
be phased out.



Does it affect your company?



If you produce goods covered by the CBAM or secondary goods using components covered by the CBAM – covered goods in the first phase:

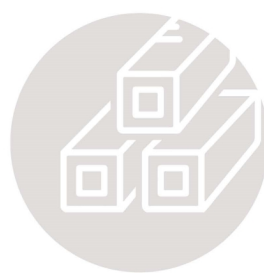
Cement



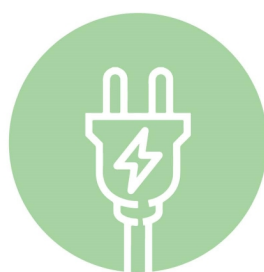
Iron & steel



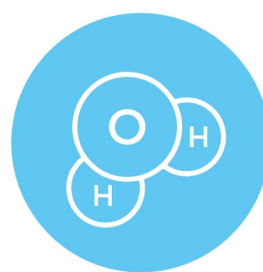
aluminium



Fertiliser



Electricity



Hydrogen



If you export goods covered by the CBAM or secondary goods with components covered by the CBAM to countries either applying the EU ETS or that are linked to it



Export



EU

Countries that are linked to the EU ETS

Countries applying the EU ETS

Based on members' feedback, the current impact on European business in China is limited. However, after the transition period, it will have larger impact especially if the scope of covered goods is expanded.

Tasks for affected companies:

Prepare quarterly reports for: embedded emissions, exported goods within the CBAM scope, the carbon price in China, and carbon intensity (starting from 1st October 2023)

Review supply chains

Calculate the financial impact so business plans can be adjusted

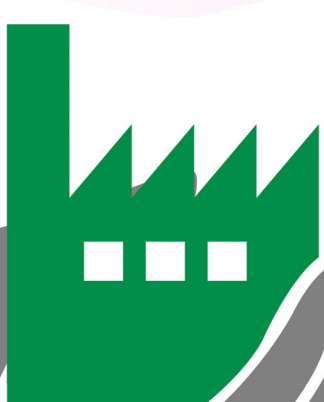
Optimise production processes to reduce emissions

Establish a management system for carbon monitoring, reporting and verification



Recommendation for all companies exporting to EU ETS countries:

Monitor CBAM developments for any changes to the scope of covered items



Frequently Asked Questions

Disclaimer: This information is provided for informational purposes only, and should not be construed as business or legal advice on any specific facts or circumstances. No users of this FAQ should act or refrain from acting on the basis of any content included, without seeking appropriate professional advice.

Q1: What will the general impact of the European Union's (EU's) Carbon Border Adjustment Mechanism (CBAM) be on China's national Emissions Trading System (ETS)?

A: While China's National ETS currently only covers the power generation sector, the introduction of the CBAM is likely to see sectors such as iron and steel, aluminium, and cement added. Their addition to the ETS would be in line with China taking steps to adjust to the CBAM.

Q2: What are some of the potential impacts of the CBAM on goods produced in China for export to the EU?

A: In the short term, the CBAM will not have a substantial impact on goods produced in China, as the country's exports of CBAM-covered products account for less than two per cent of its total exports to the EU. In fact, aluminium, iron and steel comprise almost 99 per cent of those exports, which is worth around Chinese CNY 2–2.8 billion in carbon border tax to the EU every year.²

The CBAM will have a significant impact in the longer term, as the EU transitions to full implementation in 2035. Once the CBAM coverage is expanded to all sectors under the EU ETS, it will become imperative for China to include other key emitting industries in its own national carbon market in order to reduce CBAM fees and enhance its competitiveness in an increasingly carbon-constrained world.

While the CBAM may have become a highly controversial topic, it provides a compelling argument for strengthening EU-China cooperation on decarbonisation, to ensure that the global climate agenda moves forward. A good place to start would be harmonising the standards and requirements for carbon emissions monitoring, reporting and verification (MRV).

Q3: How does China calculate emissions at the enterprise and product level, especially for multi-input and multi-output industries like iron and steel?³

A: The implementation of the CBAM requires a more accurate accounting method. Currently, the Chinese Government provides national standards for calculating enterprise-level

² How will EU's 'green tariff' impact China's carbon market?, China Dialogue, 6th February 2023, viewed 9th May 2023, <<https://chinadialogue.net/en/climate/how-will-eus-green-tariff-impact-chinas-carbon-market/>>

³ The three typical carbon accounting methods are: the actual measurement method, the emission factor method, and the input-output method. The input-output method measures CO₂ emissions by calculating the difference between inputs (fuels, materials, fluxes, etc.) and outputs (products, by-products, etc.).

emissions in major industries. A more detailed product-level standard will be updated in the next two to three years.

Q4: How do European enterprises rate China's national ETS, and how do they feel about carbon trading in China?

A: The European Chamber's *Business Confidence Survey* (BCS), released in June 2023, found that a six per cent of respondents (+1pp y-o-y) have already achieved or are near to achieving carbon neutrality. A further 52 per cent are actively taking measures to become carbon neutral, a 6pp y-o-y increase.

Meanwhile, 53 per cent of BCS 2023 respondents reported that uncertainties over China's national ETS is a top-three issue that may prevent them from achieving their decarbonisation goals in China. According to the European Chamber's report *Carbon Neutrality: The Role of European Businesses in China's Race to 2060*, released in May 2022, the Chinese authorities could make China's national ETS more effective by introducing an absolute cap on emissions, pushing up the carbon price and adopting best practices from the EU's MRV experiences.

Q5: Is there a timeline for the CBAM to expand its scope sectors?

A: There will be a review in 2025 to make extension decisions. The Commission will investigate the CBAM's extensions to indirect emissions for more sectors, as well as upstream and downstream products, but the date of the extension remains undecided.

Q6: Will the reporting obligations listed in the Implementing Regulation be the official rules for the definitive period or just temporary rules for the transitional period?

A: The transitional rules will not remain exactly the same as the rules for the definitive period but may give an indication for future rulemaking. The CBAM is not only a reflection of the EU emissions trading system (ETS) but is also an approach open to reporting from the rest of the world. The information collected during the transitional period will be used to improve the mechanism from the perspectives of the EU, foreign businesses and the authorities.

Q7: Will the EU asset verifiers be accredited by accreditation bodies in other jurisdictions?

A: Verifiers will be regulated in the definitive period but not in the transitional period. International and local verifiers with accreditations approved by any EU accreditation body will be accepted.

Q8-1: When will the default values⁴ be available and will they differ from one country to another country?

⁴ Default values are used when sufficient data on actual greenhouse gas emissions are not available.

Q8-2: Is it possible that manufacturers would use default values set in the CBAM as an excise duty to avoid investing in Monitoring, Reporting and Verification (MRV)?

A: Default values will be made available towards the end of the transitional period in 2025, and will vary between countries and sub-national regions. The Commission will publish in September 2023 a study on average emissions from all countries in the world, which will feed into the setting of default values in 2025. Data collected during the transitional period from various countries will also be used.

The possibility to use default values as a reference for the definitive period will always exist. However, producers with lower emissions would prefer to choose actual emissions rather than default values, since the latter represent the upper average of emissions.

Q9: Are International Renewable Energy Certificates (IRECs) or carbon removals allowed under the EU CBAM?

A: IRECs and carbon removals are not mentioned in the *Implementing Regulation* because the Commission tries to reflect in the CBAM what is covered in the context of the EU ETS. Other carbon pricing mechanisms may be taken into account after the recognition of a possible carbon price paid in the country of production, but this still needs to be discussed between the Commission and partner countries.