

CBAM UPDATE

PROVISIONAL DEAL REACHED POST EU NEGOTIATIONS



THE CBAM SERIES
BY
ECONOMIC LAWS PRACTICE

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Introduction

On December 13, 2022, negotiators of the Council and the European Parliament reached an agreement of a provisional and conditional nature (**Provisional Agreement**) on the Carbon Border Adjustment Mechanism (**CBAM**).¹ In continuation of our series on the CBAM (please see [here](#)), this update summarizes the key changes introduced by the provisional agreement to the operation of the CBAM.

Key Changes

a) Expanded product scope:

The original proposal for a regulation on CBAM by the European Commission was intended to initially cover the following sectors: iron and steel, cement, aluminium, fertilizers and electricity. The provisional deal expands this scope to also include **hydrogen as well as some precursors and a limited number of downstream products such as screws and bolts and similar articles of iron or steel**.

b) Emission scope:

The original proposal for a regulation was intended to cover direct emissions only. However, the provisional agreement expands the scope of emissions covered to **include indirect emissions i.e., those released during the production of goods and the electricity consumed during the production processes**. The inclusion of indirect emissions has been heavily debated as it could have significant environmental benefits but would not traditionally align with the scope of the EU ETS which does not explicitly account for indirect emissions. European industries have been largely against including indirect emissions as these could potentially discriminate against low-carbon European production because of the way in which European electricity prices are set (i.e., the marginal pricing system whereby all producers are automatically awarded the electricity price of the most expensive offer accepted).

c) Implementation Period:

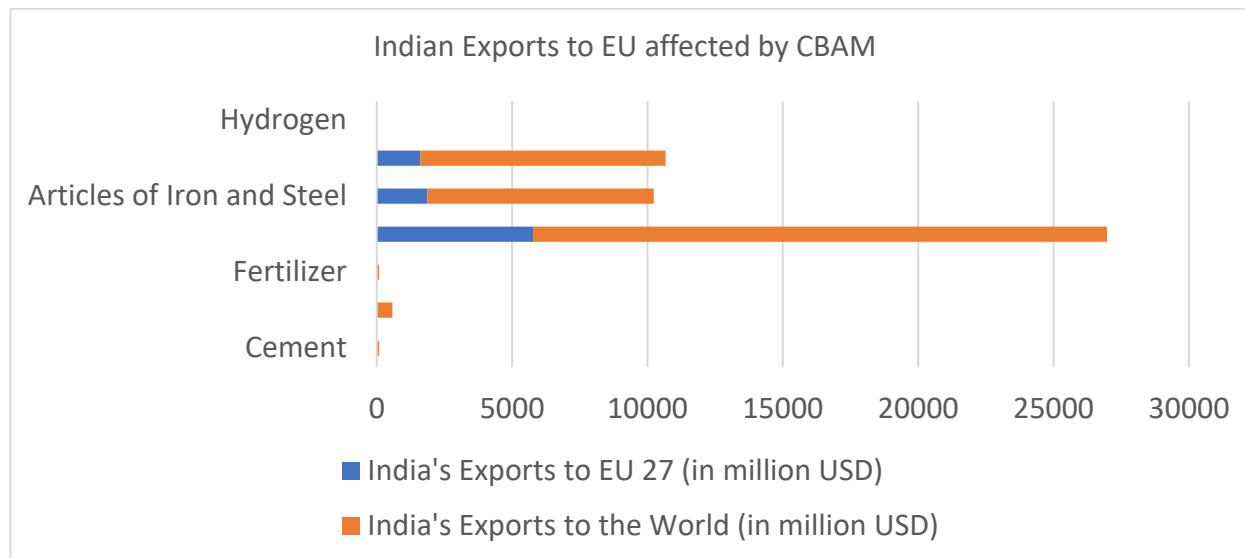
While the implementation period for CBAM was originally envisaged as beginning in January 2023, under the provisional agreement, the CBAM will begin to operate from **October 2023** whereby initially a the CBAM would apply with reporting obligations only aimed at data collection. Thereafter a full-fledged CBAM would be phased in in parallel to a phasing out of the free allowances granted to European industries under its emissions trading system. This will provide exporters with an additional period to fully understand the CBAM prior to its implementation.



¹ EU climate action: provisional agreement reached on Carbon Border Adjustment Mechanism (CBAM), European Council, available at, <https://www.consilium.europa.eu/en/press/press-releases/2022/12/13/eu-climate-action-provisional-agreement-reached-on-carbon-border-adjustment-mechanism-cbam/>

What does this mean for Indian businesses?

The imposition of the CBAM is likely to affect a significant share of India's exports to the EU. In fact, the UNCTAD forecasts that India will lose USD 1-1.7 billion in exports of energy-intensive products such as steel and aluminium.² This is in line with the general estimates provided by the Boston Consulting Group that a levy of USD 30 per metric ton of CO2 emissions could reduce profits for foreign producers by about 20%.³ A brief snapshot of India's exports in these sectors to the EU is set out below:



Source: Trade Map Data (for the year 2021)

Primarily, export baskets for the Aluminium and the Iron and Steel sector seem to be at risk. EU comprises 27.25% and 22.40% of the export basket for Iron and Steel and Articles of Iron and Steel respectively. For Aluminium, EU is the destination for 17.72% of Indian exports in the sector.⁴

In light of global tensions caused by the war in Ukraine as well as the trade war between China and the US, trade between India and the EU is expected to grow. This is further expected to expand in light of the negotiation of a free trade agreement between the two countries. Thus, the impact on Indian businesses needs to be carefully assessed and exporters would need to examine compliance.

What are the next steps?

The Provisional Agreement needs to be confirmed by ambassadors of the EU member states, and by the European Parliament, and adopted by both institutions before it is final.

Once the CBAM is in place, importers will be required to report direct and indirect emissions embedded in imported products and surrender to the EU Member State competent authorities the number of purchased CBAM certificates corresponding to the amount of verified emissions embedded in the imported CBAM goods. If the embedded emissions were subject to a carbon price in the country of origin, the importer may claim a deduction in the number of certificates to be surrendered.⁵

² EU should consider trade impacts of new climate change mechanism, UNCTAD, 14 July 2021, available at: <https://unctad.org/news/eu-should-consider-trade-impacts-new-climate-change-mechanism>.

³ Boston Consulting Group, "How an EU Carbon Border Tax Could Jolt World Trade", 30 June 2020, available at: <https://www.bcg.com/publications/2020/how-an-eu-carbon-border-tax-could-jolt-world-trade>.

⁴ Data from ITC Trade Map

⁵ Article 9 of the CBAM.

While India does not presently have an emissions trading system in place, the Indian Parliament has just approved the Energy Conservation (Amendment) Bill on December 12, 2022.⁶ The bill enables the Government to set up a domestic carbon trading scheme. The establishment of such an emissions trading system may help Indian exporters.

In the meanwhile, Indian producers will also need to establish internal systems for monitoring embedded emissions in line with the CBAM requirements. Some of the companies in India have already implemented voluntary internal carbon pricing⁷ to reduce emissions and encourage innovation in the field of a low-carbon economy.⁸ While such Indian producers already monitor their production emissions, they will need to verify the extent to which their current monitoring systems comply with the CBAM requirements.

Further clarity on the actual operation of the CBAM is expected through the issuance of the final agreement which is expected in the coming weeks. ELP will be closely following the developments in order to assess the proposed regulation from a legal, quantitative and compliance perspective.

We trust you will find this an interesting read. For any queries or comments on this update, please feel free to contact us at insights@elp-in.com or write to our authors:

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⁶The text of the bill as passed by the Lok Sabha is available at, [https://prsindia.org/files/bills_acts/bills_parliament/2022/Energy%20Conservation%20\(Amendment\)%20Bill,%202022%20as%20passed%20by%20LS.pdf](https://prsindia.org/files/bills_acts/bills_parliament/2022/Energy%20Conservation%20(Amendment)%20Bill,%202022%20as%20passed%20by%20LS.pdf)

⁷ “An internal carbon price (ICP) is a voluntarily determined price used within a company to value the cost of a unit of CO₂ e emission. This price tends to reflect the market prices of the regions where the company trades, although some companies may set theirs differently, based on their objectives.” – PUTTING A PRICE ON CARBON Handbook for Indian Companies 2.0, The Energy and Resources Institute, 2019, available at:

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⁸“Pricing carbon: Trade-offs and opportunities for India”, 5 June 2021, available at:

<https://www.orfonline.org/expertspeak/pricing-carbon-trade-offs-opportunities-india/>; What is India Inc’s carbon

footprint?, 9 July 2020, available at: <https://www.thehindubusinessline.com/opinion/what-is-india-incs-carbonfootprint/article32034375.ece>.