

# 2023 MANUFACTURING CONFERENCE

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## EU Issues Final Carbon Border Adjustment Mechanism Regulation

On May 16<sup>th</sup>, the European Union's ("EU's") final Carbon Border Adjustment Mechanism ("CBAM") regulation was published in the *Official Journal* of the EU and entered into effect. The CBAM is the EU's policy tool to "put a fair price on the carbon emitted during the production of carbon intensive goods that are entering the EU, and to encourage cleaner industrial production in non-EU countries."

### **TRANSITIONAL PHASE**

The CBAM will be implemented in two phases. First, an initial "transitional phase" will start on October 1, 2023, and run through December 31, 2025. During this period, importers of goods within the scope of the new rules, including steel,<sup>1</sup> will have to submit a report providing information on the products they have imported that are within the scope of the CBAM (see below for product list). Reports are due one month after the end of each quarter. The first report is due **January 31, 2024**. CBAM reports include the following:

- (i) The quantity of each type of good expressed in tonnes;
- (ii) Total carbon dioxide (CO<sub>2</sub>) emissions "embedded" in their imports; and
- (iii) Any carbon price due in the country of origin for the embedded emissions in the imported goods, taking into account rebates and other forms of compensation. (The EU Commission is expected to adopt a set of rules for determining how this reduction will be applied.)

*No financial payments or adjustments are required during this phase.* Instead, the transition period is intended to serve "as a pilot and learning period for all stakeholders (importers, producers and authorities)" and to collect information to help refine the CBAM methodology and program for the subsequent phase.

"Embedded emissions" include direct GHG emissions from a steel mill (commonly known as "Stage 1" emissions), as well as those associated with raw materials ("precursors") ("Stage 3 emissions"). For

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<sup>1</sup> Initially, the CBAM applies to six "carbon-intensive" industry sectors: Iron and Steel; Aluminum; Cement; Fertilizers; Hydrogen; and Electricity.

steel and several other covered industry sectors, “indirect” emissions associated with electricity consumption (“Stage 2 emissions”) are not included within the reporting requirements at this time (though may be required in the future for some sectors after the transitional phase). Details of the data reporting elements, including reporting of “precursor” emissions, will be provided in coming months through implementing regulations developed by the EU CBAM Committee.

Annex IV of the Regulation provides the methodology for calculating embedded emissions. The calculation itself is relatively straightforward:

*To determine “specific embedded emissions,” direct emissions associated with on-site production are added to the embedded emissions associated with input materials consumed during the production process, then divided by the quantity of goods produced.*

Of course, this begs the question of how to determine the embedded emissions values for input materials. The calculation should consider only input materials listed in (forthcoming) EU Commission guidance as relevant to the production process. Actual data from the raw material supplier facility (“data from the installation where the input material was produced”) should be used, “provided that that installation’s data can be adequately measured.” Absent actual data, reliable information available in the public literature may be used. In addition, the EU Commission is expected to issue guidance setting default values at the average emission intensity of each exporting country for each covered good “plus a proportionately designed mark up.”

## ***PERMANENT SYSTEM***

The core CBAM program (the “permanent” or “definitive system”) enters into force on **January 1, 2026**. By May 31 each year, importers will be required to declare the quantity of goods imported into the EU in the preceding year and their embedded GHG emissions. Importers then need to provide CBAM certificates that correspond to the embedded GHG emissions of the products brought into the EU. The price of the certificates will be calculated depending on the weekly average auction price of EU “Emission Trading System” (“ETS”) allowances expressed in Euros per tonne of carbon dioxide (“CO<sub>2</sub>”) emitted.<sup>2</sup>

### **Importer as Declarant:**

EU importers, either individually or through a representative, will have to register to be a CBAM “declarant” and buy CBAM certificates. CBAM declarants will be required to set up a CBAM account with the EU Member State of importation and, each year, surrender to that Member State the number of CBAM certificates corresponding to the level of carbon emissions embedded in the products that

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<sup>2</sup> The ETS is the existing carbon trading system for domestic EU producers. Free allowances provided to EU companies under the ETS will be phased-out in parallel with the phasing-in of CBAM during 2026-2034.

they have imported. The importer also will need to provide with its an annual declaration a verification from an accredited body. The EU Commission will be in charge of reviewing and verifying declarations as well as managing a central platform for the selling of CBAM certificates to importers.

*'Importer' means either the person lodging a customs declaration for release for free circulation of goods in its own name and on its own behalf or, where the customs declaration is lodged by an indirect customs representative ..., the person on whose behalf such a declaration is lodged.*

Importers will need to obtain information on embedded emissions for goods subject to CBAM from their non-EU producers. If such information is not available, the Regulation provides for default values on CO<sub>2</sub> emissions for each product to determine the number of certificates needed to purchase. A subsequent "reconciliation" process will allow importers to demonstrate actual emissions and amend the required number of CBAM certificates.

**Registration of Operators in Third Countries:** Article 10 of the CBAM Regulation allows operators of facilities outside of the EU to register their embedded emissions data with the EU Commission. Such registrations are valid for five years and must be supported by verification from an accredited body. CBAM declarants may use this information to fulfill their reporting obligations. This provision may be helpful to U.S. exporters, in lieu of having to provide such information to individual importers in the EU.

**Enforcement:** EU Member States are empowered to enforce non-compliance with the Regulation by imposing penalties of up to 100 Euros for each tonne of CO<sub>2</sub> for which a CBAM certificate was not provided (plus purchase of the required certificate). If covered goods are imported by a person who is not an authorized CBAM declarant, then the penalty will be three to five times higher, depending on the "duration, gravity, scope, intentional nature and repetition" of the non-compliance. The Regulation also includes provisions to prevent circumvention, defined as a "change in the pattern of trade in goods, which stems from a practice, process or work, for which there is insufficient due cause or economic justification other than avoiding, wholly or partially, any of the obligations laid down in the Regulation."

## ***LIST OF COVERED GOODS***

Annex I of the Regulation specifies that the CBAM applies to the following Iron and Steel goods falling under the EU's Combined Nomenclature ("CN") codes. For all goods, except agglomerated iron ores and concentrates, only direct (Scope 1 and 3) emissions are required to be reported; indirect emissions from electricity consumption (Scope 2) are excluded at this time. (Agglomerated iron ores and concentrates require reporting of both direct and indirect emissions.)

72 – Iron and steel

Except:

7202 2 – Ferro-silicon  
7202 30 00 – Ferro-silico-manganese  
7202 50 00 – Ferro-silico-chromium  
7202 70 00 – Ferro-molybdenum  
7202 80 00 – Ferro-tungsten and ferro-silico-tungsten  
7202 91 00 – Ferro-titanium and ferro-silico-titanium  
7202 92 00 – Ferro-vanadium  
7202 93 00 – Ferro-niobium  
7202 99 – Other:  
7202 99 10 – Ferro-phosphorus  
7202 99 30 – Ferro-silico-magnesium  
7202 99 80 – Other  
7204 – Ferrous waste and scrap; remelting scrap ingots and steel

2601 12 00 – Agglomerated iron ores and concentrates, other than roasted iron pyrites

7301 – Sheet piling of iron or steel, whether or not drilled, punched or made from assembled elements; welded angles, shapes and sections, of iron or steel

7302 – Railway or tramway track construction material of iron or steel, the following: rails, check-rails and rack rails, switch blades, crossing frogs, point rods and other crossing pieces, sleepers (cross-ties), fish-plates, chairs, chair wedges, sole plates (base plates), rail clips, bedplates, ties and other material specialized for jointing or fixing rails

7303 00 – Tubes, pipes and hollow profiles, of cast iron

7304 – Tubes, pipes and hollow profiles, seamless, of iron (other than cast iron) or steel

7305 – Other tubes and pipes (for example, welded, riveted or similarly closed), having circular cross-sections, the external diameter of which exceeds 406,4 mm, of iron or steel

7306 – Other tubes, pipes and hollow profiles (for example, open seam or welded, riveted or similarly closed), of iron or steel

7307 – Tube or pipe fittings (for example, couplings, elbows, sleeves), of iron or steel

7308 – Structures (excluding prefabricated buildings of heading 9406) and parts of structures (for example, bridges and bridge-sections, lock-gates, towers, lattice masts, roofs, roofing frameworks, doors and windows and their frames and thresholds for doors, shutters, balustrades, pillars and columns), of iron or steel; plates, rods, angles, shapes, sections, tubes and the like, prepared for use in structures, of iron or steel

7309 00 – Reservoirs, tanks, vats and similar containers for any material (other than compressed or liquefied gas), of iron or steel, of a capacity exceeding 300 l, whether or not lined or heat-insulated, but not fitted with mechanical or thermal equipment

7310 – Tanks, casks, drums, cans, boxes and similar containers, for any material (other than compressed or liquefied gas), of iron or steel, of a capacity not exceeding 300 l, whether or not lined or heat-insulated, but not fitted with mechanical or thermal equipment

7311 00 – Containers for compressed or liquefied gas, of iron or steel

7318 – Screws, bolts, nuts, coach screws, screw hooks, rivets, cotters, cotter pins, washers (including spring washers) and similar articles, of iron or steel

7326 – Other articles of iron or steel

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