



## **Inception Impact Assessment: Carbon Border Adjustment Mechanism (CBAM)**

### **Response of AEGIS Europe**

AEGIS Europe is an industry alliance that brings together more than 20 European manufacturing associations committed to manufacturing in the EU on a truly level playing field ensured by a rules-based free and fair international trade. Our members account for more than €500 billion in annual turnover, as well as for millions of jobs across the EU. We support the goal of the European Union to fight climate change and make Europe the most sustainable economy globally. To achieve those goals, it is essential to put in place policies which strengthen the Union's manufacturing industry and keep EU manufacturing value chains competitive.

We ask the Commission to consider the points expressed below in designing a proposal for any CBA mechanism. As a preliminary comment, and in the light of the current health and sanitary emergency and the economic crisis that will follow in the EU, it will be essential to adapt decarbonisation policies to the new context, in particular to avoid the collapse of productive systems and social cohesion throughout the EU.

1. Fundamentally, a CBA mechanism must be designed so as to contribute to the objective of decarbonisation in the EU by strengthening and completing existing measures protecting European industries from the risk of "carbon leakage", or the risk of relocation of manufacturing and investment. Accordingly, free allocations should be maintained as a complement to border measures to avoid all forms of carbon leakage. On the other hand, it must be recognised that for some sectors, CBAs may not be appropriate and complementary measures in addition to free allocations and indirect costs compensation should be considered. The underlying aim is to ensure the equal treatment of all products placed on the EU market with regard to the limitations and costs of decarbonisation measures.

- The CBA mechanism must in principle apply regardless of the country from which a product is imported. For example, the CBA must apply to products from a given country regardless of the preferential status of that country under EU legislation and/or the designation of that country as a developing country by a multilateral institution.
- The CBA mechanism must reflect the cap or limitation on EU carbon emissions as well as the costs for those emissions which are permitted.
- A carbon border mechanism must not replace, and *a priori* any transitional period of CBA application must not endanger, existing direct and indirect EU carbon leakage measures, including ETS free allowances and indirect costs compensation.

- A CBA mechanism designed in this manner can then provide strong incentives for third countries to decarbonise local manufacturing, and reach a common approach with the EU on carbon pricing and related issue.

2. This implies that:

- A CBA mechanism must not only consider the carbon footprint of imports but also reflect the overall carbon footprint of making those or similar products in the places where the essential manufacturing steps take place. Thus, while a CBA mechanism must in principle be based on the actual carbon footprint of imported products, i.e. not a simple average benchmark or *ad valorem*, other policies may be relevant in setting the carbon cost to be imposed on imports.

Measuring the carbon footprint of imports and reflecting the total manufacturing emissions in the places where the essential manufacturing steps take place requires a proper and efficient system of measurement, with incentives and sanctions to maximise the cooperation of importers and their third country suppliers. In cases where data is not made available in a timely and complete manner, or cooperation is otherwise materially deficient, default values should be used which do not allow an opportunity for free-riding. The general acceptance of on-site verification visits at the places where essential manufacturing steps take place must be considered a fundamental requirement for cooperation.

- While full carbon accounting should, in principle, ultimately cover the entire value chain, upstream and downstream, from the primary raw materials and other inputs (including energy) down to final end products, and include transport to the EU port of final destination, a transitional approach with a border measure focused on the most carbon-intensive steps is a practicable starting point. Full carbon accounting in turn will require a robust analysis of the whole supply chain for each sector to capture sectorial specificities and needs, especially during any transitional period.
- A CBA mechanism must provide for appropriate and efficient cost adjustments to address trade flow manipulations such as source shifting and CBA absorption. This is an essential element to ensure the effectiveness of a CBA in tackling carbon leakage.
- Any steps taken to simplify measurements must not significantly increase the risk of CBA avoidance. In addition, the CBA mechanism must provide sufficient scope for adjustments to address any inadequacy that arises or becomes evident after implementation.
- To have a coherent focus on products placed on the EU market and to ensure proper incentives for third countries to reach a common approach with the EU on carbon pricing, any CBA should not result in the impairment of the competitiveness of EU exports to third countries.

3. While the minimisation of additional administrative burdens is important, an effective CBA mechanism requires a legitimate and robust monitoring, reporting and verification (MRV) system for collecting and disclosing the direct and indirect emissions in the production of the affected products.

4. Also, while CBA enforcement would naturally be entrusted to Member States, there need to be sufficiently detailed rules at EU level to ensure the availability of timely information and the application of effective and dissuasive Member State measures to penalise avoidance.

5. Throughout the process of putting in place a comprehensive CBA mechanism, transparency and close dialogue with trading partners will be important. However, the EU must not be held hostage to delays in finding agreement before putting in place a fully functioning CBA mechanism. In addition, the EU must:

- be prepared to defend fully its CBA mechanism under existing international agreements, including the WTO Agreements, without backing down in the face of unilateral pressures from third countries;
- not revise the CBA mechanism in the context of agreement on bilateral or multilateral instruments that are only meant to support “green” technologies/products (e.g. Environmental Goods Agreement) or achieve other aims besides comprehensive and effective carbon pricing across borders;
- ensure that third country carbon pricing and limitation arrangements are effectively implemented, and compatible with EU arrangements (i.e. impose similar costs and limitations for a similar carbon footprint in a given sector), before agreeing to make any linkages with the systems of those third countries.

6. To be coherent with the objective of the CBA, and EU climate policy objectives in general, funds raised from the CBA should be used primarily to encourage research and innovation in carbon-reducing technologies related to manufacturing and facilitate their application in the EU.

7. The upcoming CBA impact assessment should be an integral part of a broader discussion between the EU institutions and all the stakeholders potentially concerned. In particular, the design of a CBA proposal should not be detached from the discussion and implementation of the New Industrial Strategy for Europe. At the same time, the elaboration of a CBA proposal should not pre-empt the strengthening and development of other EU policy instruments which can contribute to mitigating the risk of carbon leakage through a fair level playing field in relation to the many environment- or health and safety-related costs borne by the EU manufacturing sector but not fully by producers outside the EU.

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