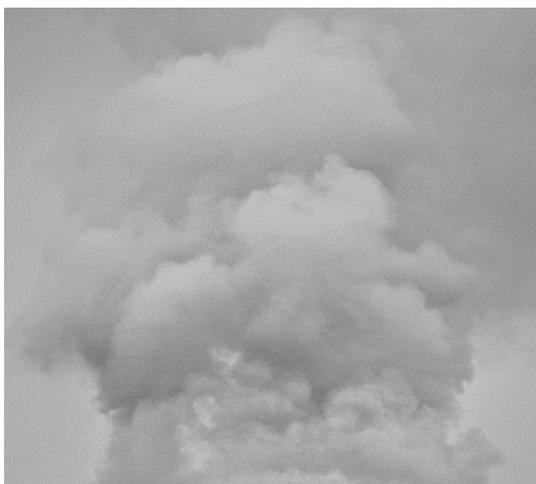


## Energy taxes/ Customs

### Carbon border adjustment mechanism (CBAM)

Over the past decade, and due to the will of the European Union (hereinafter referred to as the EU) to reduce emissions of fluorinated greenhouse gases, the prices of emission allowances in the European Union Emissions Trading System (hereinafter EU ETS) have increased, creating an uneven playing field for European emission-intensive industries competing in global markets.

In this respect, the Union's intentions have been offset by an increase in emissions outside its borders, as a result of the relocation of production to non-EU countries, or by the increase in imports of carbon-intensive products, thus creating a risk of carbon leakage.



In this context, the European Commission (hereinafter EC) presented on 14 July 2021 a proposal for a Regulation of the European Parliament and of the Council establishing a carbon border adjustment mechanism

(hereinafter, CBAM), with which it is intended to match the carbon price paid for EU products operating under the EU ETS and for imported products.

This will only be possible by forcing companies importing into the EU to buy so-called CBAM certificates, in order to pay for the difference between the carbon price paid in the country of production and the carbon price in the ETS.

The CBAM Regulation is part of the *Fit for 55* package of measures and is an essential element in achieving EU climate neutrality by 2050.

Although CBAM reflects certain aspects of the EU ETS in terms of costs and compliance, it is a standard that sets out its own procedures and administrative structure.

The proposal for a Regulation outlines a decentralised approach delegating certain essential functions and their implementation to the Member States' authorities, subject in any case to supervision and coordination by the European authorities.

Thus, this Regulation published in July 2021, establishes general guidelines, which are being negotiated by the Member States.

In the meetings held during the week of 13 to 18 December 2022, MS approved an

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Interim Agreement with the Council to create the CBAM, which states that it will enter into force from 1 October 2023.

Initially, it is foreseen the application of a transitional period in which information obligations are established for the importer, whereas the duration of this transitional period and, therefore, the full introduction of CBAM, will be linked to the progressive elimination of free allowances in the framework of the EU ETS, scheduled for until 2026, when CBAM will begin full operation.

Next, we will expose the main characteristics of this mechanism:

#### 1.- Objective scope

CBAM is intended to apply to goods originating in third countries and listed in Annex I, which are imported into the customs territory of the Union.

However, Annex II lists the countries and territories not covered by the Regulation, namely Büsingen, Helgoland Island, Livigno, Ceuta and Melilla.

Such products would be iron and steel, cement, aluminum, fertilizers and electricity. Provision is made for an extension, on a proposal from MS to hydrogen, indirect emissions under certain conditions, certain precursors and certain derived products, such as

screws and bolts and similar articles of iron and steel.

Additionally, the Council and Parliament have agreed to end free allowances for these sectors within nine years, between 2026 and 2034.

During this time, CBAM will only apply to the production of broadcasts that do not benefit from free allowances under the EU ETS, in order to fully respect the rules of the World Trade Organization.

#### 2.- Roles and responsibilities

The administration of the annual compliance obligations of this mechanism involves a number of authorities and stakeholders, both within the EU and in third countries exporting the covered products to the EU.

##### i) *Competent authorities*

Each MS shall designate a competent authority which shall be the principal institution responsible for the implementation of the mechanism. The competent authority in many MS for CBAM is likely to be the same as the competent authority responsible for the EU ETS, as the tasks require similar capabilities.

The tasks of the competent authorities relating to this mechanism shall be as follows:

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- To authorize declarants to import CBAM goods into the EU; and opening an account for each filer in the national registry.

- Receipt and review of CBAM declarations; calculation and, if necessary, adjustment of CBAM certificates.

- Enforcement and management of disputes with declarants, and imposition of penalties for non-compliance by declarants, including during the transitional phase, on those who do not report their direct and indirect emissions.

- Establishment and maintenance of a computer system to monitor the operations covered by the CBAM.

#### *ii) Customs authorities*

They will be responsible for allowing the importation of goods covered by CBAM. Such goods may enter the European market only if a declarant is authorised by a competent authority.

In this context, the customs authorities shall be responsible for communicating the import information to the competent authority of the MS in which the declarant is established and has already obtained the authorisation, including his identification number (EORI number),

the account number CBAM, the classification number of the goods covered by the CBAM, the country of origin of the goods and the quantity of goods.

#### *iii) Respondents*

In the proposal for a Regulation of EC, importers are referred to as declarants and must apply to the competent authority of their place of establishment for approval.

This is a precondition for importing any of the goods covered by the CBAM Regulation, which are defined using the EU classification system at customs, the Combined Nomenclature (CN). The CN is based on the international Harmonized System (HS), which is applied in most countries. EU customs rules require declarants to be legally established in the EU to lodge a customs declaration, which is often done through agents acting as customs representatives.

In the case of declarants who, at the time of lodging the application, have been established for a period of less than two financial years, the competent authorities may require the lodging of a security fixed at the maximum value of the CBAM certificates to be issued.

In order to cover the implicit emissions of imported goods subject to CBAM, authorised declarants shall purchase and

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deliver CBAM certificates, which shall be marketed by the competent authority of each Member State at a price calculated in accordance with the procedures laid down in Regulation (EU) n° 1031/2010 for each calendar week.

Before 31 May of each year, respondents must submit what is known as a "CBAM declaration" to the competent authority that authorized them.

The CBAM declaration shall contain the total quantity of each type of product imported during the previous calendar year, the total integrated emissions of the products and the total number of CBAM certificates to be delivered, less any redemption for a carbon price that has already been found. paid in the country where the goods were produced and an adjustment to take account of duties allocated free of charge to EU installations producing CBAM goods.

An authorized declarant who does not comply with the obligation to deliver within the prescribed period the number of CBAM certificates corresponding to the emissions implicit in the goods imported during the previous year shall be subject to a penalty of EUR 100 for each tonne of carbon dioxide equivalent emitted by the installation for which the operator has not delivered the CBAM certificate. relevant, increased by EUR 40 for each CBAM certificate that the

authorized declarant should have delivered.

However, during the transitional phase, declarants will only be obliged to report, having no financial obligations.

For each quarter of the year, they must submit a "CBAM report", detailing the amount of each type of good they imported, the actual total direct emissions incorporated, the actual total indirect emissions embodied and the price of carbon owed in the country of origin for the goods.

Although, with regard to indirect emissions from imported goods, whereas in the transitional phase declarants will be obliged to report such emissions, the proposed EC Regulation in 2021 does not currently impose compliance obligations on indirect emissions during the operational phase from 2026 onwards.



#### *iv) Operators in third countries*

Facilities operating in third countries and exporting their goods to the EU for import by declarants will not face any formal

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obligation under the proposed EC regulation.

However, in order to be able to sell goods to the EU, they will have to provide the declarant with product-specific information on embedded emissions, including detailed records of the information necessary for their calculation and a verification report prepared by an accredited verifier.

v) *The European Commission*

In the proposed Regulation, the CE will act as "central administrator" to maintain an independent record of CBAM certificate transactions. Thus, the CE is responsible for ensuring the coordination of the records maintained by the competent authorities.

In addition, it will carry out checks on recorded transactions to detect possible irregularities, which may be due to both fraudulent behaviour and accidental errors in national registers.

In the same vein, CE will be responsible for addressing the circumvention of CBAM. Circumvention means a change in trade patterns motivated primarily by an attempt to circumvent CBAM, for example by importing slightly modified products that do not fall within the scope of CBAMs.

The CE will also be responsible for adopting several implementing acts

necessary for the establishment and harmonization of CBAM procedures.

This includes key issues such as the methodology for reducing CBAM obligations based on carbon costs in the country of origin, specifying the control and supervision conditions of accredited verifiers through national accreditation bodies, and establishing detailed rules to determine embodied emissions from covered goods.

vi) *Emission verifiers and national verifier accreditation bodies*

Declarant shall ensure that the emissions attributable to the goods notified in their annual CBAM declarations were independently verified by an EU ETS verifier or by a CBAM accredited verifier.

While the obligation to report the total number of embedded emissions lies with importers (declarants), emissions subject to verification are those resulting from production processes at facilities in third countries. Therefore, much of the verification work will be done outside the EU.

Verifiers shall be accredited in accordance with the existing regulation on verification of emission verifiers for the EU ETS (Implementing Regulation 2018/2067), which establishes harmonised standards and procedures

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for verifiers together with the accreditation process.

The CBAM Regulation also lays down verification principles, such as compulsory visits to installations in third countries except under certain conditions, which are similar to the obligations laid down in the current Community legislation on emission verification.

### 3.- Term of application

The Provisional Agreement approved by MEPs with the Council on December 13, 2022, establishes that proposal CBAM will enter into force on October 1, 2023, with a transitional period until 2026, in which there will only be the obligation to report.

In this context, the guidelines on control and notification, as well as the provisions on penalties in the event that the declarant fails to comply with his obligation to inform, should be adopted as an implementing act by October 2023, as should the necessary communication channels between competent authorities and customs authorities, and IT channels.

### 4.- Conclusions

To conclude this analysis, it is useful to make a summary of the main

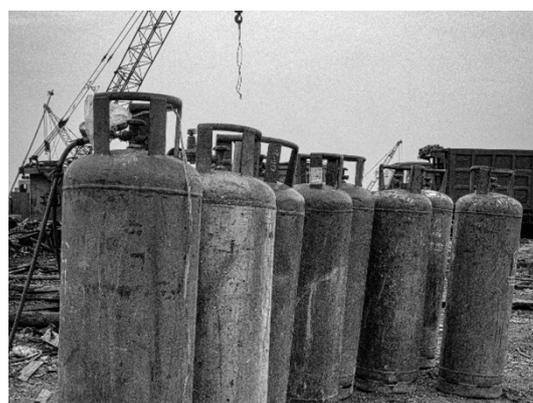
developments introduced with this mechanism:

- For the sectors concerned, the CBAM will cover iron and steel, cement, aluminium, fertilisers and electricity, as proposed by the European Commission. MS agreed to extend the target scope to hydrogen, certain by-products (e.g. screws and bolts) and indirect emissions under certain conditions.

- The transitional phase will start in October 2023, during which importing companies will only have the obligation to inform. The implementation of the tax will not take place until 2026.

- Currently, the EU allocates free allowances to European carbon-intensive industries to cover part of their emissions and thus help them compete with foreign industries.

However, as CBAM is implemented, these rights will be phased out. The elimination of those rights will not, in principle, take place until 2026.



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We hope that these comments will be useful. For more information, please feel free to contact any of us at the following email addresses.

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