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As of 1 October 2023

The EU Carbon Border Adjustment Mechanism (CBAM) Enters into Force

The regulation on the Carbon Border Adjustment Mechanism (CBAM) was published in the Official Journal of the European Union on 16 May 2023 and entered into application on 1 October 2023. The first reporting period for importers will end on 31 January 2024. At the initial stage, the EU will apply this regulation to imports of products and intermediate goods from sectors with carbon-intensive production and a high risk of carbon leakage, such as **cement, iron and steel, aluminium, fertilisers, electricity, and hydrogen**. The scope will later be expanded and integrated into the EU Emissions Trading System (EU ETS).

Purpose and Objectives of CBAM

While pursuing its climate objectives, the EU aims to align all economies with this direction. Climate change is a major global challenge, and effective solutions can only be achieved through cooperation among all economies and by addressing the issue with equal importance. In this context, the EU has introduced the Carbon Border Adjustment Mechanism (CBAM) to prevent the risk of carbon leakage that may arise from the relocation of production to non-EU countries with less stringent climate policies, as well as from the import of carbon-intensive products, while at the same time safeguarding the competitiveness of EU-based companies.

For this purpose, a carbon pricing mechanism similar to the EU ETS, which has been in place since 2005, has been designed. Accordingly, CBAM foresees the application of carbon pricing at the import stage for products falling within its scope. In summary, by assigning a fair price to the carbon emitted during the production of imported carbon-intensive goods, the EU aims to protect domestic producers, encourage non-EU companies to invest in and adopt more environmentally friendly production practices, and achieve its emission reduction targets more rapidly.

Background and Scope

CBAM was first presented by the European Commission on 14 July 2021 as part of the “Fit for 55” package. Fit for 55 is a component of the European Green Deal, which serves as the EU’s roadmap in line with the objectives of the Paris Agreement. The package covers energy, transport, land use, taxation, and climate policies and aims to reduce greenhouse gas (GHG) emissions by 55% by 2030 compared to 1990 levels.

In this framework, CBAM is a regulatory instrument introduced to combat climate change, preserve the competitiveness of Member States, and encourage them to establish carbon pricing policies. By aligning the cost of imported carbon-intensive products with that of domestically produced goods under climate policies, the mechanism aims to reduce emissions. The current list of carbon-intensive products and goods will be expanded over time.

In addition, to prevent the risk of carbon leakage in offshore installations, the Commission is expected to be granted authority to establish requirements for the application of CBAM to goods or products derived from goods located in fixed or floating structures, artificial islands, or structures situated on the continental shelf or in the exclusive economic zones of Member States, as well as in adjacent areas to the Union customs territory.

Timeline of the Process

- 14.07.2021 – Proposal submitted by the European Commission
- 15.03.2022 – EU Council adopted its approach
- 22.06.2022 – European Parliament approved the CBAM proposal
- 10.05.2023 – CBAM Regulation signed
- 16.05.2023 – Published in the Official Journal
- 17.05.2023 – Entry into force
- 01.10.2023 – Application date
- 31.01.2024 – End of first reporting period
- 01.01.2026 – Full implementation date

TRANSITION PERIOD	END OF TRANSITION PERIOD	FULL IMPLEMENTATION
01.October.2023	**31.December.2025**	**2026-2034**
Priority Products and Intermediate Goods: Cement, iron and steel, aluminium, fertilisers, electricity, hydrogen ***First Reporting Deadline*** 31.January.2024	Payment obligations and scope expansion	Gradual integration into the EU ETS

What Are the Transitional Period Requirements?

Upon the proposal of the European Commission, the period between 1 October 2023 and 31 December 2025 has been defined as the transitional phase. During this period, importers will be required to report emissions related to goods covered by CBAM without making any financial payments. This phase is designed primarily to understand the system, ensure accurate declarations, generate data, and facilitate the subsequent surrender of certificates.

Importers must report greenhouse gas emissions associated with the carbon-intensive products they import without making payments or adjustments. During this phase, free allocations will be introduced. These allocations will be calculated based on the emission quantities declared by the importer. Importers will be able to purchase CBAM certificates from the Commission in advance. These certificates must correspond to the declared emissions and cover the relevant imports for the reporting period. The Commission will verify the accuracy of the reported emissions and may request information from customs authorities when necessary.

Information Required in the Reports

- Product, installation, and country of origin information; quantity of each product; detailed electricity consumption (MWh) and tonnage for other products
- Embedded emissions for each product
- Indirect emissions for each product (in accordance with the implementing regulation to be published)
- Net carbon emissions of the product (after payments, offsets, or compensations in the country of origin)

During the transitional phase, third-party greenhouse gas verification will not be required. CBAM will initially apply to carbon-intensive products and intermediate goods, with the scope to perceive more than 50% of emissions in sectors that will later be included in the ETS. New implementing rules are expected.

In summary, before full implementation, the transitional period is crucial for understanding the system, completing necessary preparations, collecting data, identifying and addressing deficiencies, deepening learning, ensuring compliance with CBAM, and enabling accurate declarations.

When Will Full Implementation Begin?

Following the completion of the transitional period, CBAM will enter into full implementation on 1 January 2026 and will be integrated into the EU ETS. The gradual inclusion of CBAM into the EU ETS and the phase-out of free allocations have been designed to occur simultaneously. During this period, imports of goods covered by CBAM will only be carried out by authorised CBAM declarants established in the EU. Import procedures may be conducted directly or through indirect representatives (customs brokers).

At this stage:

- Importers will be required to purchase CBAM certificates when importing CBAM-covered goods. The price of embedded carbon

emissions will be equivalent to the carbon price of goods produced under EU carbon pricing rules.
- If the imported product is subject to a similar system (ETS) in its country of origin, it may be exempt from the EU ETS. Upon declaration by the producer, the corresponding cost will be deducted.
- Accordingly, CBAM is expected to incentivise non-EU countries to take environmentally friendly actions aimed at reducing carbon costs.

Although compliance obligations fall on EU importers, they will request all necessary information regarding reporting, monitoring, and verification (as of 2026) of embedded emissions from producers. Therefore, exporters producing the relevant goods will need to address Scope 1, 2, and 3 emissions in accordance with the regulation. Exporters should also verify in 2025 whether their EU-based importers have obtained authorised CBAM declarant status.

Globally, similar mechanisms are planned in countries such as Canada and Japan, while the IMF and OECD are working on how international actions can support greenhouse gas emission reductions. In California, this mechanism is already applied to certain electricity imports.

How Will CBAM Operate?

According to the agreement reached, the European Commission will be responsible for ensuring the proper functioning of CBAM and coordinating among competent authorities of Member States. The Commission will actively manage all processes.

CBAM will operate similarly to the EU ETS. Importers will be required to purchase CBAM certificates, the price of which will be calculated based on the weekly average auction price of EU ETS allowances (€ per tonne of CO_2). Importers must register individually or through representatives to obtain CBAM certificates. Importers wishing to bring CBAM-covered goods into the EU must, by 31 May each year, declare the quantity of goods imported in the previous year and their embedded emissions, and surrender the corresponding CBAM certificates purchased in advance from the Commission. For 2026, the first surrender deadline will be 31 May 2027.

Key Differences Between CBAM and the EU ETS

- While both the EU ETS and CBAM pursue common greenhouse gas reduction objectives and share similar mechanisms, CBAM focuses on the carbon intensity of imported goods rather than imposing a cap on emissions.
- Other distinguishing features include certificate pricing, trading, and validity periods, as CBAM prioritises preventing carbon leakage over carbon trading.

- Administrative and operational flexibility may be considered an advantage for SMEs.
- To ensure effectiveness, CBAM prices are designed to closely align with EU ETS prices, using the weekly average of EU ETS auctions to mitigate price volatility.
- While the EU ETS covers specific production processes and activities, CBAM focuses on the import of goods.
- Unlike the EU ETS, the regulation does not impose a cap on the number of CBAM certificates, aiming to reflect EU ETS price developments and prevent carbon leakage, while allowing importers to optimise costs through the purchase of excess certificates.

How Will CBAM Certificate Prices Be Determined?

According to the regulation:

- The Commission will calculate the price for each calendar week based on the average closing prices of EU ETS allowance auctions.
- If no auction takes place in a given week, the last auction price will be used.
- The calculated average price will be published on the relevant website on the first working day of the following week and will apply for the entire week.
- The Commission is the sole authority responsible for adopting implementing acts regarding the methodology and practical arrangements.

Emissions Covered by CBAM and the Scope of Emission Calculations

As specified in Annex I of Directive 2003/87/EC, CBAM covers greenhouse gas emissions including carbon dioxide, nitrous oxide, and perfluorocarbons. Accordingly, emission calculations must include perfluorocarbons for aluminium and nitrous oxide for fertilisers.

While CBAM initially accounts for direct emissions embedded in imported goods, indirect emissions will also be included for certain products. Indirect emissions arise from electricity generation used in the production of covered goods. Including indirect emissions is expected to enhance environmental and climate outcomes. However, due to specific cost measures for electricity, indirect emissions will initially not be included in the embedded emission calculations for iron and steel, aluminium, and hydrogen (Annex I-A). Methodologies for calculating indirect emissions are expected to be defined during the transitional period. After this period, indirect emissions for products such as cement, fertilisers, and agglomerated iron ores are expected to be included based on a defined methodology.

What Are the Penalties?

Failure to comply with obligations during both the transitional and full implementation phases will result in penalties. The regulation outlines the following sanctions:

1. Importers who fail to surrender the required CBAM certificates corresponding to embedded emissions of goods imported in the previous year by 31 May will be subject to penalties equivalent to the excess emissions penalty under Article 16(3) of Directive 2003/87/EC, increased in accordance with Article 16(4) applicable in the year of import.
2. It is prohibited for goods to be released into the Union customs territory by a person other than the authorised CBAM declarant without fulfilling the obligations.
3. Payment of penalties does not exempt importers from surrendering the required CBAM certificates.
4. Unpaid penalties will be recovered in accordance with the laws of the relevant Member State.

Conclusion

The EU remains firmly committed to its 2050 net-zero target and, within the framework of the European Green Deal, is compelling all economies to align with increasingly stringent and complementary regulations. The first major test will occur in 2030. If the transitional target of reducing emissions by 55% compared to 1990 levels is not achieved, stricter measures will follow. Therefore, all economies and businesses must promptly develop roadmaps under the issued directives to ensure continuity and competitiveness by the 2030–2032 sustainable transition period.

This regulation represents one of the most concrete examples of this framework. Full implementation will begin in 2026, reinforcing the 2030 targets. Exporters should aim to achieve better emission performance than EU producers in the production of CBAM-covered goods by reducing emissions across Scope 1, 2, and 3. Sectors and businesses unable to adapt to the transition process will face sustainability risks.

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