Energy & Environment Working Group

Newsletter
TOPIC OF THE MONTH

ITALY CHINA COUNCIL FOUNDATION
意大利中国理事基金会

GLOBALIZING CARBON PRICE

CBAM AND ITS IMPACT ON THE EU-CHINA TRADE

With the Regulation (EU) 2023/956 dated May 10th 2023, the Carbon Border Adjustment Mechanism (CBAM) has become a reality with which the importers of the products included in the scope of application of the Regulation shall confront, and the downstream production chain shall deal with upon forecasting their costs' structure.

The rationale of the measure is in line with the European Green Deal: embedding the cost of GHG emissions within current production costs, in such a way as to discount costs that market mechanisms would otherwise burden only on the States (with innumerable resilience and remediation interventions) and on future generations.

focus
CBAM GOODS

IRON AND STEEL
ALUMINUM
ELECTRICITY
CEMENT
FERTILIZERS
HIDROGEN

Additional goods shall be assessed during the transitional period

CBAM shall operate in close coordination with the EU Emission Trade System (ETS), the "cap and trade" mechanism that compels heavy emitters to cap their emissions and to purchase emissions allowances, which can be traded among emitters which exceed their quota and virtuous emitters which do not reach it.

The impact of the mechanism on costs has been so far limited by the EU by means of releasing a number of free allowances on the market, a practice that is going to be progressively phased out, while CBAM is implemented. On one side, relevant EU heavy emitters will see the carbon price rise in the EU due to the reduction of free allowances, at the same time they shall face a fairer market situation thanks to CBAM: importers of goods in the same field of those EU heavy emitters covered by ETS, will be obliged to purchase CBAM certificates, when importing goods from countries where carbon emissions are not priced or are priced at a lower level with respect to EU.

EU AND NON-EU PRODUCTS SHALL THUS CIRCULATE ON THE EU MARKET, ALL EMBEDDING A LEVELLED CARBON PRICE.

The further purpose of CBAM is to prevent **carbon leakage** and thus to jeopardize the EU efforts towards decarbonization.

A side effect of the ETS and of delocalization into countries with less stringent climate objectives, could in fact be the global increase of GHG emissions, which CBAM intends to prevent.

KEY CONCEPTS

CARBON LEAKAGE
Transfer of carbon-intensive production to countries with less-ambitious climate policies, to avoid costs' increase due to ETS mechanism and, in particular, to the phasing out of free allowances

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TIMING AND OBLIGATIONS

According to the CBAM Regulation, a **transitional period** will allow progressive introduction of obligations: **from October 1st 2023 to December 31st 2025**, CBAM goods' importers shall be subject to reporting obligations only.
No financial payment shall be made. **The first reporting shall be made within May 31st 2027, with respect to the CBAM goods imported during the IV quarter of 2026.**

The transitional period shall allow both the EU and non-EU businesses to align with the new procedures and to make adequate forecasts in terms of impacts and of the actions to be taken. At the same time the EU shall have the time to implement the legal framework by issuing an implementing regulation.

As of January 1 2026 Importers of CBAM goods shall register with the competent national authorities and declare:

- the direct and indirect emissions embedded in the CBAM goods they import (to be certified by a qualitied entity); should the relevant exporter fail to provide such information, the EU shall fix default values to be used for reference;

- the carbon price prospectively paid in the country of origin.

With respect to the emissions not "paid" at goods' origin, the importer shall purchase CBAM certificates, which shall thus operate as allowances for the unpaid emissions, thus levelling the burden of carbon price on all CBAM goods on the EU market.

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DIRECT AND INDIRECT EMISSIONS

Direct emissions, are those generated upon production of a given good.
Indirect emissions are those generated upon generation of the energy consumed to produce such goods.

For **iron and steel, aluminum and hydrogen** the Regulation currently indicates that only direct emissions shall be considered.

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WHAT SHALL BE THE PRICE OF CBAM CERTIFICATES?

A CBAM certificate shall cover 1 ton CO_2 and its price shall be the weekly average auction price of a EU ETS allowance for 1 ton CO_2.

In this manner, all operators dealing with the same CBAM goods will result to have paid a uniform price for the embedded emissions, being them EU operators within the ETS or extra-UE operators subject to CBAM.

CHINA'S POSITION ON CBAM

As global champion of green strategies and investments, China looks at CBAM with a dual approach: the potential virtuous impact of CBAM on the global carbon pricing trend is clearly recognised; on the other hand, China itself has set up a carbon quota trading system, which is preparing to become the most important globally. However, at the same time, the local press often refers to the CBAM as the **green barrier raised by the EU to protect its businesses.**

The EU is further accused by China of having adopted a unilateral measure, in contrast with the WTO practice of multilateral agreements. Despite the above, differently with respect to India, who threatens a recourse to WTO against CBAM, China has so far not challenged – at least not too vigorously – compliance of CBAM to WTO rules.

China's doubts are of course focused on the prospective price increase for Chinese economic operators who export to the EU as well as on the impact that the new European Regulation will have on developing countries and their exports to the EU.

So far, though, the prevailing approach seems to be one of waiting: Chinese attention is focused on the ways in which the introduction of the CBAM certificates will actually be accompanied by the phasing out of the free allowances under the ETS in the EU, on the price of CBAM certificates and on the methods of calculating the emissions embedded in the CBAM Products. **Trasparency and fairness of such process will be carefully monitored.** These aspects in the making, could therefore have a significant influence on the future's approach of China towards CBAM.

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TO DO LIST AND PREPARATION ACTIONS

For extra-UE exporters.
Chinese exporters of CBAM goods may obtain the registration of their extra-UE installations in the CBAM register hold by the Commission. To this purpose, extra-UE exporters shall collect a number of information, which require dedicated preparation and understanding of the EU requirements: Chinese exporters shall implement an internal monitoring system of emissions generated by their productive activities and the relevant data shall be collected and certified on the basis of Regulation 2018/2067.
In such manner, the emissions embeded in the CBAM goods exported to the EU shall be predetermined, thus simplifying the relevant import procedure for EU importers.

For EU importers.
They shall apply for the status of authorized CBAM declarant, to be entitled to carry out imports of CBAM goods. Besides, they shall liaise with the Chinese suppliers of CBAM goods, in order to assess:

- their availabiility to proceed with monitoring and calculating relevant direct emissions and electricity consumed.

- the carbon price paid in China for the CBAM products, in order to be ready to claim deduction of such paid carbon price against CBAM obligations. China has established its own ETS, which covers a number of CBAN goods: the allowances paid under the Chinese ETS shall be deductable from those to be purchesed under CBAM. However, the two ETS are not alligned in terms of esmissions' price, therefore such calculation of paid and unpaid carbon price shall still be performed.

EU has committed to foster the development of **IT tools**, the organization of **dedicated training** and preparation of **explanatory documentations**, so as to spread the know how needed to deal in an efficient manner with CBAM procedures. It shall be EU importers and China exporters' duty to acquire such knowledge to be ready to fulfill the upcoming reporting obligations and to face actual implementation phase of CBAM.

In the meanwhile, **assessment of businesses' carbon emission**, above all for CBAM products, is no more an option to be met under non binding / binding ESG requirements of EU and China's relevant legal framework. Through introduction of CBAM, the carbon footprint of products has become an essential KPI on which all impacted businesses shall closely focus.