

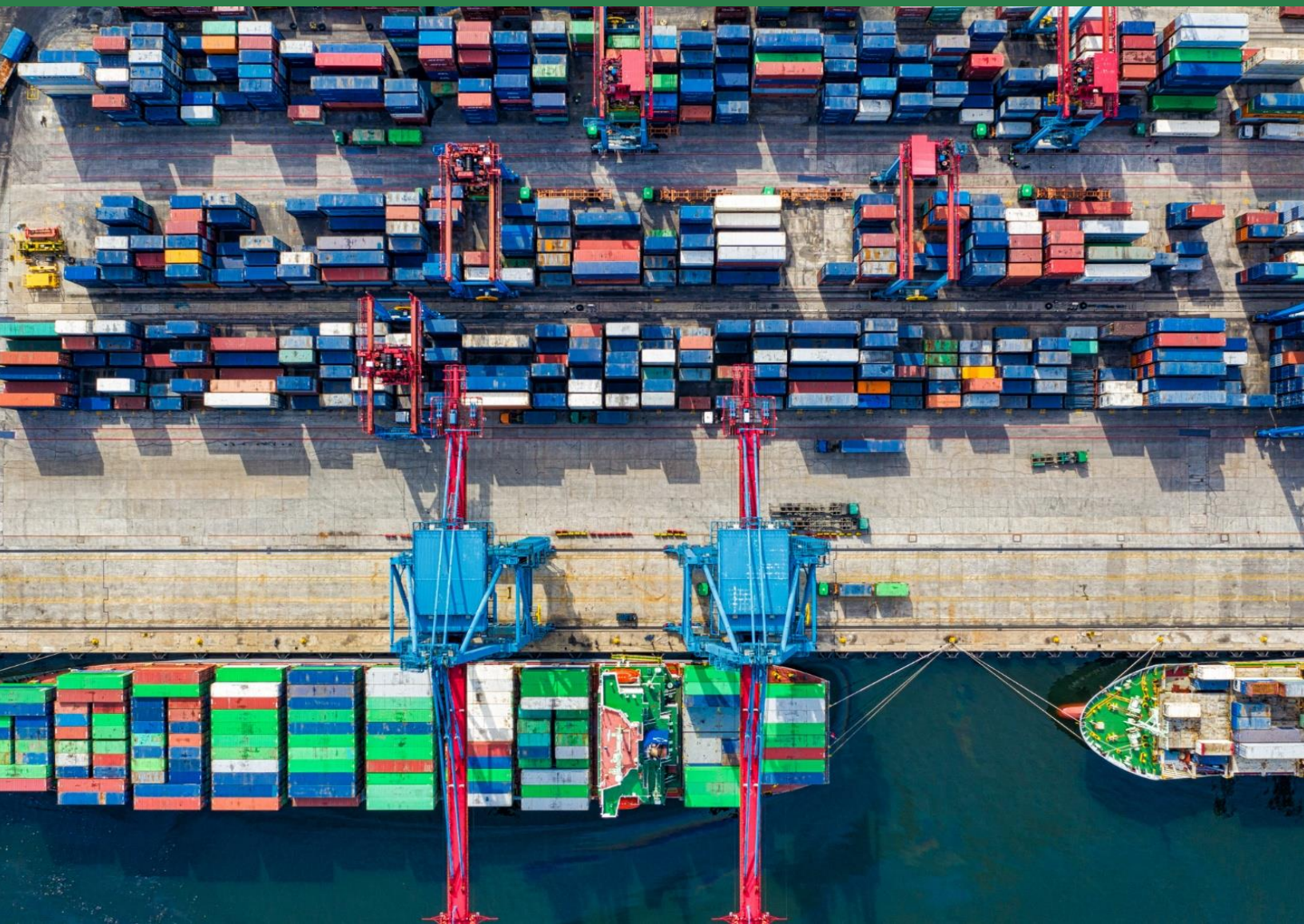


ERCST

Roundtable on
Climate Change and
Sustainable Transition

2026

Response to the Q4 2025 CBAM Legislative Proposal



Andrei Marcu Michael Mehling Aaron Cosbey Marco Sangiovanni Helen Bevernage

SUMMARY

- *The December 2025 legislative package engages with several longstanding design questions as the CBAM enters its definitive phase, including, among other topics, anti-circumvention, downstream scope extension, the treatment of third-country carbon prices, export-related leakage, and introducing a new safeguard mechanism under Article 27a.*
- *The proposals represent an important step in the operationalization of the CBAM and an effort to make it fit for purpose, but multiple elements show unresolved trade-offs between environmental ambition, administrative feasibility, and regulatory predictability.*
- *The credibility and effectiveness of the mechanism will depend heavily on how the forthcoming implementing acts and the upcoming ETS revision address the remaining gaps.*

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1 Introduction

The European Roundtable on Climate Change and Sustainable Transition (ERCST) is an independent think-tank dedicated to facilitating informed debate and providing analysis of European Union (EU) and international climate policy. Its work has consistently focused on the functioning of carbon pricing instruments, including the EU Emissions Trading System (ETS) and the Carbon Border Adjustment Mechanism (CBAM). Across multiple publications and stakeholder dialogues, ERCST has examined the conceptual foundations of border carbon adjustments, the nature and evolution of carbon leakage risk, competitiveness implications for European industry, and the practical conditions required for policies to remain environmentally effective, legally defensible, and administratively workable.

Building on the earlier phases of the project Border Carbon Adjustments in the EU, this paper constitutes ERCST's effort to accompany the CBAM as it evolves from a legislative framework to a mechanism operating in practice. The movement from transitional arrangements towards the definitive phase comes in parallel with an increase in attention to how its detailed rules, governance structures, and implementation choices interact with market realities, international partners, and domestic political expectations.

On 17 December 2025, the European Commission presented a legislative package amending and complementing the CBAM ahead of the start of its definitive phase on 1 January 2026. The package included, as its principal components, the Proposal for a Regulation amending Regulation (EU) 2023/956 as regards the extension of its scope to downstream goods and anti-circumvention measures (*COM(2025)989*), and the Proposal for a Regulation establishing the Temporary Decarbonisation Fund (*COM(2025)990*). In parallel, the Commission has been advancing a number of Implementing and Delegated Acts addressing methodological, verification, administrative, and enforcement aspects of the legislation. Taken together, they represent a significant update to the CBAM framework.

Against this background, the objective of the present paper is to assess how certain of the measures put forward by the Commission relate to the stated purposes of the CBAM and to the broader policy logic that has guided its development to date. The intention is not to reopen foundational debates, but rather to situate the new proposals within the trajectory of earlier design choices and analytical reflections. In doing so, the paper wishes to identify areas of convergence with previous ERCST work, highlight where uncertainties or tensions may persist, and indicate aspects that could merit further attention as implementation unfolds.

In line with this approach, the paper examines specific issues covered by the proposal. In particular, the analysis addresses:

- the proposed measures to **lower the risk of circumvention**, including the distinction between illegal avoidance of obligations and behavioural responses that arise within the boundaries of the rules (e.g., *resource shuffling*);
- the proposal to **extend CBAM coverage further downstream** along the steel and aluminium value chains;
- the pending measures to have **CBAM credit for carbon pricing systems in third countries**;

- the proposed measures to address **exposure of export-oriented production to residual carbon leakage risks** as free allocation under the ETS is progressively reduced;
- **Article 27a** – “Exclusion in case of serious and unforeseen circumstances”.

While some of the issues above reflect longstanding areas of debate, the legislative package delivers concrete institutional details that allow in-depth assessment beyond what could previously be undertaken. As well, it introduces a new governance element through Article 27a. This provision allows for the temporary exclusion of goods from the CBAM scope in situations characterised as serious and unforeseen circumstances affecting either the functioning of the mechanism or the supply of goods on the Union market. As a novel feature within the CBAM architecture, it requires dedicated examination.

2. Analysis

2.1 ERCST Assessment Criteria

2.1.1 Definition of carbon leakage

Broadly speaking, carbon leakage occurs when emission reductions in countries resulting from stricter greenhouse gas mitigation policies are partially or completely offset by emission increases in countries that apply less stringent policies¹. According to the Commission², the term ‘carbon leakage’ refers to the transfer of CO₂ emissions from one country to another when, due to strict climate policies, companies relocate their production to countries with weaker emission constraints which may or may not contribute to an increase in global greenhouse gas emissions. The formula for calculating it is the emissions increase in other countries divided by the emissions reduction in the implementing country, expressed as a percentage:

$$\text{Carbon leakage} = \frac{\text{Emission increase in non – EU regions}}{\text{Emission reduction in the EU}}$$

- The reduction in emissions in the EU may result from a reduction in production within the EU or from a reduction in demand for the products concerned.
- There are multiple dimensions and channels of carbon leakage including:
 - **Production leakage:** whereby the asymmetry of climate policies between the EU and other countries leads companies to relocate production or reduces their market share vis-à-vis imports and exports.

¹ For instance, the IPCC Fifth Assessment Report defines leakage as the “*phenomena whereby the reduction in emissions (relative to a baseline) in a jurisdiction/sector associated with the implementation of mitigation policy is offset to some degree by an increase outside the jurisdiction/sector through induced changes in consumption, production, prices, land use and/or trade across the jurisdictions/sectors*”. Source: p.125, IPCC, 2014: Climate Change 2014: Synthesis Report. Contribution of Working Groups I, II and III to the Fifth Assessment Report of the Intergovernmental Panel on Climate Change [Core Writing Team, R.K. Pachauri and L.A. Meyer (eds.)]. IPCC, Geneva, Switzerland, 151 pp. <https://archive.ipcc.ch/report/ar5/syr/>

² European Commission. (2021). Impact Assessment Report accompanying the document Proposal for a regulation of the European Parliament and of the Council establishing a carbon border adjustment mechanism. SWD(2021) 643 final. Part 1, Table 4. <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52021SC0643>.

- **Investment leakage:** similar to production relocation, companies redirect their investments to countries with less stringent climate policies to avoid associated carbon costs.
- **Exports leakage:** this refers to the carbon leakage risk associated with goods manufactured in the EU for export, arising from the competitive disadvantage and potential loss of market share on the global market that EU producers may face due to higher carbon costs.
- **Value chain leakage:** this refers to the displacement of carbon leakage risk to downstream value chains when climate measures such as an ETS cover the upstream.
- A figure greater than 100% would mean that carbon leakage actually caused global emissions to increase. For perspective, the Commission’s impact assessment of the CBAM modelled a complete removal of free allocation without a protective CBAM and predicted leakage in the CBAM sectors of 42%.³ Emissions reduction in the EU that appear in the denominator of the leakage formula can stem from different mechanisms, including demand destruction. Carbon leakage below 100% does not necessarily equate to a desirable outcome – while it is not as harmful in terms of global emissions, it is harmful economically as it would lead to EU de-industrialization, and harmful environmentally because it would thereby lead to erosion of support for climate policies.

2.1.2 CBAM objectives

The definition of carbon leakage outlined above provides the analytical foundation for understanding the objectives of the CBAM, as well as putting forward a framework to gauge its performance. As noted in Article 1(1) of Regulation (EU) 2023/956⁴, the CBAM is established “to address greenhouse gas emissions embedded in the goods listed in Annex I on their importation into the customs territory of the Union in order to prevent the risk of carbon leakage, thereby reducing global carbon emissions and supporting the goals of the Paris Agreement, also by creating incentives for the reduction of emissions by operators in third countries.”

Preventing carbon leakage is the key explicitly stated objective in the CBAM Regulation. However, the wording of Article 1 also reflects additional objectives connected with the “*thereby*”/ “*and*”, which allow for an increasingly broader interpretation: the narrow product-level focus, the broader producer/sector-level focus on competitiveness, and the overarching global-level objective concerning environmental outcomes:

- **Address carbon leakage by ensuring that the EU domestic carbon price is mirrored on the carbon intensity of imports at product level.** This understanding would only require that goods actually entering the EU face a symmetrical carbon cost but would not affect the remaining share of foreign producers’ output.
- **Address carbon leakage and competitiveness by ensuring that the effective carbon price in an exporting country is mirroring the EU domestic carbon price on carbon**

³ European Commission. (2021). Impact Assessment Report accompanying the document Proposal for a regulation of the European Parliament and of the Council establishing a carbon border adjustment mechanism. SWD(2021) 643 final. Part 1, Table 4. <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52021SC0643>.

⁴ Regulation (EU) 2023/956 of the European Parliament and of the Council of 10 May 2023 establishing a carbon border adjustment mechanism, Article 1, para. 1. <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32023R0956>

intensity at the sector level. This interpretation goes beyond the first by providing a more comprehensive approach to safeguard the competitiveness of EU producers and ensure comparable treatment of imports and domestic production.

- **Preventing an overall increase in global GHG emissions:** Under a global-level interpretation, the CBAM's purpose would go beyond ensuring competitive parity or carbon cost symmetry between EU and foreign producers. Instead, the central objective would be to prevent an overall rise in global GHG emissions. In this view, carbon leakage is understood as a situation where the EU carbon pricing leads to an increase in emissions outside the EU that offsets the reductions achieved within the EU.

2.1.3 Criteria for analysing the proposed amendments

In order to examine how the December 2025 proposals contribute to these objectives, ERCST will assess them in the following sections against a set of five criteria:

- **Governance and legal implications:** Do the proposed provisions comport with established principles of good governance? Do they respect the EU's internal and international legal obligations?
- **Political feasibility and external implications:** Do the proposed provisions strike a careful enough balance of benefits and costs among stakeholders – both domestic and international – to be politically viable?
- **Technical feasibility:** Do the proposed provisions avoid undue administrative complexity? Are they feasible in practice?
- **Environmental implications:** Do the proposed provisions achieve the CBAM's objectives, whether conceived as reducing the risk of carbon leakage or as lowering global GHG emissions?
- **Competitive implications:** Do the proposed provisions achieve the CBAM's objective, if conceived as protecting the competitiveness of EU industry?

2.2 Anti-Circumvention

2.2.1 Commission measures

Summary of legal changes introduced:

- Inclusion of pre-consumer scrap of aluminium and steel as CBAM-covered precursors with non-zero embedded emissions (but not covered as goods per se).
- Commission empowerment to further detail CN codes to capture the composition of products within certain CN codes, where there is risk of mis-declaration of composition and thus GHG intensity.
- Commission empowerment to require additional proof of time and place of production for goods and origins, where there is risk of mis-declaring installation-based origin of imports.
- Commission empowerment to require additional evidence demonstrating that abusive practices have not occurred, where there is deemed to be high risk.

Key objectives stated by the Commission

The overall objective for the changes proposed is to “tackle attempts to avoid the CBAM obligation” whether through “misdeclaration of emissions intensities”, or through “abusive practices”.⁵ A slightly different formulation of the objective is laid out in the impact assessment report:

“Reducing the risk that CBAM importers and/or third country operators employ practices for which there is insufficient due cause or economic justification, other than to effectively unduly avoid, wholly or partially, the financial liabilities arising from CBAM without a genuine reduction in GHG emissions.”⁶

The Commission’s impact assessment summarizes four specific cases of avoidance that the proposed measures should address:

1. The “scrap loophole”. Since scrap inputs to steel and aluminum are assessed at zero embedded emissions, there is an inequity: domestic pre-consumer scrap faces a passed-through carbon price, but the same foreign scrap would face none. Goods made with such scrap material, then, are not on an even playing field.
2. The potential to mis-declare actual emissions intensity, given the wide variation of emission intensities that can exist within the existing CN codes (e.g., cement with or without high levels of clinker fall under the same CN code, but have widely different GHG intensities).
3. The potential to mis-declare the installation-level origin of goods, where different installations may have very different emissions profiles.
4. The risk of “abusive practices” more broadly, defined as “an actor ... gaining a benefit by unduly avoiding, wholly or partially, the CBAM financial liability and thereby undermining the effectiveness of the CBAM to address the risk of carbon leakage in the EU.”⁷

It is worth noting that the fourth measure can only be internally consistent with the objective enunciated above if we accept that “unduly” avoiding CBAM liability means doing so without “due” cause or economic justification. This is unclear. In particular, it is not clear whether the carbon price that is the CBAM should be considered “due” cause or economic justification for foreign firms responding to that carbon price, for example by investing in clean production for export to the EU, or directing their existing (now competitive) clean production to the EU rather than their (now less competitive) dirty production.

New tools, powers, or definitions introduced

5 European Commission. (2025). “Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2023/956 as regards the extension of its scope to downstream goods and anti-circumvention measures” COM(2025) 989 final, pp. 1-2.

6 European Commission. (2025). “Impact Assessment Report Accompanying the Document ‘Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2023/956 as regards the extension of its scope to downstream goods and anti-circumvention measures.’” SWD(2025) 988 final. P. 20.

7 European Commission. (2025). “Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2023/956 as regards the extension of its scope to downstream goods and anti-circumvention measures” COM(2025) 989 final, Article 1(3).

The new elements proposed correspond to the challenges outlined above:

1. Pre-consumer steel and aluminium scrap should be listed as a CBAM precursor, by means of addition to Annex I of the CBAM regulation.
2. The Commission should be empowered to further detail CN codes to better capture the specific composition of certain goods that, within the same CN code, are characterized by a wide range of GHG intensity.
3. The Commission should be empowered to adopt implementing/delegated acts to attach additional conditions to the use of actual emissions data for certain goods and origins—such as proof of time and place of production—where it is determined that there is high risk of abusive practices. These might include mis-declared emissions intensity, for example by mis-declaring installation-level origins of imports, or by mis-declaring the specific composition of the imported goods. Or they might include other as-yet unspecified types of behaviour, given the broad definition of abusive practices noted above.

Enforcement and monitoring mechanisms envisaged

Under the proposals, the Commission shall monitor for evidence pointing toward a high risk of abusive practices for a combination of goods and origins.⁸ Where this is found, the Commission shall within three months adopt delegated acts on the identification of goods and origins for which additional evidence is to be included in the CBAM declaration, as well as the specific type of evidence to be provided.

2.2.2 ERCST assessment

- **Governance and legal implications:** Including pre-consumer scrap as a precursor in CBAM coverage might at first blush appear to violate WTO non-discrimination principle, since EU producers are not liable for ETS allowances based on the embedded emissions in the scrap inputs they use. However, the argument for including scrap is similar to the argument for including any upstream inputs in the CBAM: producers using those inputs may not have to pay a carbon cost *directly*, but they do pay the carbon cost as passed through by the upstream installations that produced those inputs.

The decision not to include post-consumer scrap was made in part to align with internal EU practice as pending under the Circular Economy Act. Imposing CBAM charges on post-consumer scrap would dis-incentivize the collection and recycling of post-consumer steel and aluminum in trade partners, in contrast to the coming prioritization of such efforts within the EU under the draft Act.

Empowering the Commission to act on abusive practices without better defining such practices is one way to try and address the issues given uncertainty about future efforts to circumvent the CBAM and the difficulties in defining circumvention; it creates flexibility for reactive remedial action. But at the same time, it introduces critical legal uncertainty about what practices will be allowed. It could be argued, for example, that a low-GHG-intensity foreign installation that pivots to export to the EU because of CBAM's carbon

⁸ European Commission. (2025). "Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2023/956 as regards the extension of its scope to downstream goods and anti-circumvention measures" COM(2025) 989 final, Article 1(5)(c).

pricing incentives is engaging in abusive practices, per the definition above offered in the impact assessment.⁹ But such behaviour is a normal market reaction to a carbon price. Uncertainty about what practices are “abusive” might stifle foreign investment in clean production that otherwise would have taken place.

- **Political feasibility / implications:** From a domestic perspective, all of the proposals for anti-circumvention are politically feasible; they are likely to be welcomed by most EU producers, and have few significant implications for EU consumers.

Downstream steel and aluminium processors, however, may be less welcoming of the changes. They will see their input costs rise as any raw and semi-finished inputs made with foreign scrap would be more costly.

Internationally, some aspects of the proposals will not be welcomed. For those countries and sectors that are deemed to be at high risk of mis-declaring actual emissions, or for those that might be deemed at high risk of other unspecified abusive practices, the new requirements will be an increased cost of exporting to the EU, both in terms of compliance and in terms of mandated use of punitive default values. In both cases, foreign producers will struggle to estimate their exposure, since the criteria are not clear.

- **Technical feasibility:** Closing the scrap loophole is legally straightforward; it involves simply listing pre-consumer scrap in the Regulation’s Annex I. It will, however, be technically challenging to determine how much such scrap was incorporated in any given import of processed steel or aluminium, and for those same imports verifying how much pre-consumer vs post-consumer scrap was used. It may also be technically challenging to enforce any new CN codes at the border. The physical characteristics of the imports themselves will not be helpful in distinguishing among any new sub-classifications.
- **Environmental implications:** Disaggregating CN codes would help prevent carbon leakage if it worked in practice (note the technical challenges cited above), as would requiring more information on time and place of production of certain covered imports. Both would help prevent circumvention via mis-declaration of embedded emissions.

It is not clear what environmental impact the provision on abusive practices would have, since it is not clear what sorts of practices it would prevent beyond mis-declaration. In the worst-case scenario, this provision would be used to address resource shuffling – that is, used to prevent clean foreign producers from responding to the carbon price imposed by CBAM. Such a scenario would disincentivize foreign producers from decarbonizing investment. Moreover, if clean foreign producers were somehow penalized at the point of import—for example by forcing the use of default values—it could even result in higher overall global emissions of GHGs.

Including pre-consumer scrap in the CBAM as an input would help prevent leakage among secondary steel and aluminium producers and downstream processors in two related ways: it would even the playing field such that foreign producers face the same carbon costs as do domestic producers (who face it as a passed through cost – see the section on

⁹ This practice of rearranging trade flows in response to a carbon price such as CBAM is known as resource shuffling, and has been the subject of strong calls for preventative action by EU producers. See Marcu et al. (2025). “The EU CBAM in Practice: The Challenge of Resource Shuffling”. ERCST. <https://ercst.org/the-eu-cbam-in-practice-the-danger-of-resource-shuffling/>.

competitiveness implications below); and it would prevent foreign producers from intentionally mis-declaring high amounts of input scrap.

Not covering *post*-consumer scrap in the proposed scope extension would leave some potential for leakage from those same two sources: carbon cost differential, and the risk of mis-declared high use of such scrap. This environmental cost would need to be balanced against the fact that including post-consumer scrap in the CBAM coverage would disincentivize recycling of steel and aluminium at the national or firm level in trading partners, by treating such scrap no better than primary metal.

- **Competitive implications:** Disaggregating CN codes would help protect the competitiveness of EU producers if it worked in practice (note the technical challenges cited above), as would requiring more information on time and place of production for specific goods and origins. Both would help prevent circumvention via mis-declaration of embedded emissions. The increased compliance burden this would place on all affected foreign producers would also accord an advantage to competing EU producers.

Similarly, covering pre-consumer scrap as inputs under CBAM would protect the competitiveness of EU steel and aluminium producers by leveling the playing field with foreign producers not facing a carbon cost. EU producers will face that cost because pre-consumer scrap is typically used at or close to the site of production, which means in the EU it will include a passed-through carbon price.

The dynamic is different for post-consumer scrap, which arguably does not include a passed-through carbon price. However, the prices of scrap aluminum (whether pre-or post-consumer) and to a somewhat lesser extent scrap steel, track the prices of primary product, being close substitutes. That means that in the EU prices of scrap will increase, whether they are covered by CBAM or not, because primary production is covered and free allocation is being phased out. In effect, then, post-consumer scrap poses the same uneven playing field problems that pre-consumer scrap does, and its lack of coverage in the proposal leaves a gap in protection against loss of competitiveness.

For both pre- and post-consumer scrap, coverage under CBAM would also help prevent unfair competition via mis-declaration. Here again, the lack of coverage for post-consumer scrap is a problem, especially as it is difficult to determine accurately the proportions of pre- and post-consumer scrap that may have been used in foreign production.

If the abusive practices provisions were used to prevent resource shuffling, for example by denying the ability to use actual data for embedded GHGs, there would be clear competitiveness benefits conferred on EU producers.

2.2.3 Areas of alignment with ERCST analysis

ERCST has highlighted the problem of the “scrap loophole” in previous reports¹⁰, but has not made recommendations on whether both pre- and post-consumer scrap should be covered under CBAM.

¹⁰ Marcu et al. (2025). “The EU CBAM in Practice: The Challenge of Resource Shuffling”. ERCST. <https://ercst.org/the-eu-cbam-in-practice-the-danger-of-resource-shuffling/>; Marcu et al. (2025). “Future of Emissions Trading in the EU: EU ETS – CBAM Strawman”. ERCST. <https://ercst.org/future-of-emissions-trading-in-the-eu-eu-ets-cbam-strawman/>

If the abusive practices provisions were used to address resource shuffling, that might conflict with ERCST recommendations that counsel against restricting the submission of actual data as a means to address the problem.¹¹

2.2.4 Looking forward

Upcoming implementing acts or guidance

In the course of implementing the proposals outlined above, should they be accepted, the Commission would need to undertake the following:

- Elaborate a definition of new CN codes.
- Create a potential phased in mark-up value for scrap of aluminum or steel.
- Enact a delegated act that outlines how to determine where there is risk of mis-declaring the installation-based origin of imports, and what type of additional information to require in such cases.
- Enact a delegated act on what else might constitute evidence of abusive practice, the information/evidence to be required where such evidence is present, and legal requirements for Commission to act on such findings.

Recommendations

The proposed efforts to identify cases where there is risk of mis-declaration—disaggregated CN codes and additional burden of proof of place and time of production—are a step in the right direction, but they should be implemented in a balanced way, cognizant of the burden of compliance that they entail for covered foreign producers, some of which would inevitably be innocent of any misconduct.

The provisions to include scrap as CBAM-covered input goods with non-zero embedded emissions should also include post-consumer scrap. Granted, this may mean less incentive for foreign governments to implement aluminium and steel recycling and circularity programs and regulations. But the EU is not such a major global market that this effect would be determinative. Such coverage would remove the technically difficult challenge of trying to accurately determine how much post-consumer scrap was used in the making of any given good, eliminating the possibility of strategic mis-declaration. And it would even the playing field in terms of carbon cost paid by domestic and foreign producers.

The provisions on abusive practices represent an untested approach to addressing an issue that carries significant risk for EU industry. If this instrument is to command the confidence of those that must rely on it, it will need to be tested and substantially clarified.

They should be elaborated in such a way to ensure that they will not be used to address resource shuffling, which ultimately is avoidance—normal market behaviour—not circumvention. As we have recommended elsewhere, the risk of resource shuffling is more appropriately addressed by extending the timeline for the phase-out of free allocation, and using the interim to double down

¹¹ Marcu et al. (2025). “The EU CBAM in Practice: The Challenge of Resource Shuffling”. ERCST. <https://ercst.org/the-eu-cbam-in-practice-the-danger-of-resource-shuffling/>

on support for the competitiveness of low-carbon industrial production in the EU.¹² Further, the Commission should establish procedures that would allow public input as an element of the monitoring and enforcement regime, similar to the channels offered to private sector complainants to urge initiation of anti-dumping or subsidy investigations.

2.3 Article 27a

2.3.1 Commission measures

The December 2025 legislative package introduced a new provision, Article 27a, establishing the possibility for the temporary exclusion of goods from the scope of the Carbon Border Adjustment Mechanism under specific exceptional conditions. Under the proposed text, where the Commission, taking into account the relevant evidence, considers that the inclusion of a good in Annex I causes “*severe harm to the Union internal market due to serious and unforeseen circumstances related to the impact on the prices of goods*”, it is empowered to adopt delegated acts in accordance with Article 28 to remove that good from Annex I until those serious and unforeseen circumstances have passed.

The structure of the provision therefore links three cumulative elements: (i) severe harm to the internal market, (ii) the existence of serious and unforeseen circumstances, and (iii) a connection between those circumstances and impacts on the prices of goods. In practical terms, this enables the temporary removal of goods listed in Annex I from CBAM coverage where these conditions are met. The Commission has clarified that the rationale of the provision is to allow intervention in situations that could not reasonably have been anticipated at the time of adoption and that risk destabilising the internal market. To operationalise this safeguard, Article 27a empowers the Commission to adopt delegated acts specifying the goods concerned and the timing of their exclusion. An urgency procedure is foreseen to allow for rapid response where necessary. The Commission has further indicated that, where justified by the timing of the disturbance, such measures could apply with retroactive effect from the moment the relevant conditions are considered to have been met (*Q&A on new Article 27a - January 8th, 2026*).

At the same time, the proposal emphasises that exclusions should remain temporary and targeted. Their duration is linked to the persistence of the circumstances that justified intervention, implying that once those conditions no longer exist, normal CBAM application would resume.

2.3.2 ERCST assessment

The introduction of Article 27a represents a significant change in the governance architecture of the CBAM. By creating a legal avenue through which goods may be temporarily removed from the scope of the mechanism, the proposal introduces a new provision that impacts regulatory stability and flexibility, in exceptional situations. It joins with other areas of EU regulation that have been granted or have asked for exemptions.

We assess such provision under the criteria defined above.

- **Governance and legal implications:** From a governance perspective, Article 27a establishes an important precedent. Until now, the scope of CBAM coverage has been

¹² Ibid.

anchored in primary legislation, with modifications subject to the ordinary legislative process. The possibility of exclusions through delegated acts introduces a more agile instrument, but also one that relies on a significant degree of Commission discretion. The effectiveness of such a mechanism will depend heavily on how clearly the triggering conditions, standards, and procedural steps are defined. In this regard, the provision establishes a cumulative threshold: the Commission must, taking into account the relevant evidence, determine that the inclusion of a good causes severe harm to the Union internal market due to serious and unforeseen circumstances related to the impact on the prices of goods. The reference to price impacts therefore introduces a more specific legal benchmark within the broader assessment of internal market harm. At the same time, the concepts of “severe harm” and “serious and unforeseen circumstances” remain open-textured legal standards. Their interpretation will depend on how thresholds of harm are defined, how evidence is assessed, and how the causal link between price developments and internal market effects is established. If these elements remain open to interpretation, the provision will generate uncertainty for market participants regarding the durability of obligations and the reliability of long-term investment signals. Conversely, overly rigid criteria could limit the ability of the safeguard to respond to genuine emergencies.

The prospect of retroactive application, as acknowledged by the Commission, adds a further layer of complexity. While it may be justified in circumstances where market disturbances precede formal intervention, it raises questions regarding legal stability.

- **Political feasibility and implications:** The availability of an exclusion mechanism is also likely to influence the political dynamics surrounding CBAM implementation. Sectors experiencing price pressures or supply constraints may perceive Article 27a as an avenue through which relief could be sought. Given the explicit reference to price impacts in the provision, arguments grounded in increases in domestic market prices may become a focal point of political mobilisation around the activation of the safeguard. This may be particularly relevant in markets characterised by strategic importance, high import dependency, or strong domestic sensitivities. While such flexibility may improve the resilience of the system in times of crisis, it may also create expectations among stakeholders that CBAM coverage can be adjusted in response to economic difficulties. The way in which requests for intervention are handled will therefore be central to maintaining confidence in the stability of the mechanism.
- **Technical feasibility:** From an operational standpoint, the activation of Article 27a appears feasible. The Commission already possesses mechanisms for adopting delegated acts, and customs and administrative authorities are accustomed to implementing changes in tariff or regulatory treatment when required. However, practical challenges may arise in ensuring that exclusions are communicated, applied and, where necessary, reversed in a consistent manner across Member States, particularly if retroactivity is involved.
- **Environmental implications:** Any temporary removal of goods from CBAM coverage carries an inherent environmental trade-off. By suspending the carbon price signal at the border, the mechanism may reduce incentives for emission reductions associated with the affected products and could increase exposure to leakage during the period of application. The extent of this risk will depend on the duration, scope and frequency of the exclusions. At the same time, failure to respond to severe disruptions could generate political or

economic reactions that might ultimately weaken support for the CBAM more broadly. The environmental assessment must therefore consider both the immediate impact of an exclusion and its longer-term implications for the credibility of the system.

- **Competitive implications:** Finally, differentiated treatment across goods or time periods may create distortions between operators. Firms competing in closely related markets could face divergent cost structures depending on whether their products fall within or outside an exclusion decision. Predictability regarding the conditions and duration of interventions will therefore be important in limiting unintended competitive effects.

2.3.3 Areas of alignment with ERCST analysis

Several elements of the approach reflected in Article 27a resonate with positions that ERCST has consistently emphasised in earlier phases of its work. In particular, the recognition that the CBAM must remain operable under changing economic conditions aligns with the view that implementation frameworks require a degree of responsiveness in order to maintain political durability. At the same time, ERCST has repeatedly underlined that flexibility should not come at the expense of predictability. Investment decisions, contractual arrangements and supply strategies depend on a reasonable expectation regarding the stability of regulatory requirements. From this perspective, the emphasis placed in the proposal on the temporary and targeted nature of possible exclusions corresponds to a longstanding ERCST recommendation that any deviation from standard application must be clearly bounded in time and governed by transparent procedures.

The introduction of Article 27a therefore seeks to provide a mechanism for situations that may be politically and economically disruptive, but as currently drafted, the provision leaves considerable room for interpretation which could be eliminated. Whether it succeeds in practice will depend on how the provision and its triggering conditions are specified and applied.

2.3.4 Looking forward

As attention turns to implementation, several aspects of Article 27a would benefit from further clarification in order to ensure coherent application across Member States and to provide adequate visibility for operators.

- **Clarifications required:** In particular, greater precision may be needed regarding the criteria that would trigger the activation of the safeguard, the methodology for assessing whether the threshold of serious and unforeseen circumstances has been met, and the factors determining the scope and duration of any exclusion. Additional guidance may also be necessary to explain how such measures would interact with existing CBAM obligations, especially in cases where retroactive application is envisaged. Clarifying these elements would contribute to reducing uncertainty, facilitating administrative preparedness and strengthening confidence in the governance of the mechanism.
- **Monitoring and future evaluation:** Given the novelty of the instrument, the manner in which Article 27a is used in practice will require close observation. The frequency of interventions, the sectors concerned and the duration of exclusions will provide important indications regarding how the safeguard affects the overall stability and credibility of the CBAM. Future assessments may also need to consider the impact of such measures on affected industries, on trade patterns, and on the incentives for decarbonisation both within and outside the Union.

Recommendations

In light of these considerations, ERCST considers it essential that the operationalisation of Article 27a is accompanied by clearly defined conditions, robust procedural safeguards and transparent decision-making processes. Providing timely information to operators and Member States will be essential in maintaining predictability. At the same time, the safeguard should remain exceptional in character. Reliance on exclusions as a recurring response to structural market challenges would weaken the integrity of the CBAM and dilute the incentives that the mechanism is intended to create.

Since this type of provision is implemented for EU sectors and circumstances, it should be seriously considered when such circumstances also occur in exporting countries.

2.4 Carbon Prices in Third Countries

2.4.1 Commission measures

The legal basis for recognising carbon prices effectively paid in third countries remains anchored in Article 9 of Regulation (EU) 2023/956 (CBAM Regulation), which provides for a reduction of the CBAM obligation corresponding to a carbon price “effectively paid” in the country of origin:

“An authorised CBAM declarant may claim in the CBAM declaration a reduction in the number of CBAM certificates to be surrendered in order to take into account the carbon price paid in the country of origin for the declared embedded emissions. The reduction may be claimed only if the carbon price has been effectively paid in the country of origin. In such a case, any rebate or other form of compensation available in that country that would have resulted in a reduction of that carbon price shall be taken into account.”¹³

Article 3(29) of the CBAM Regulation defines “carbon price” in relatively narrow terms, referring to explicit pricing instruments such as emission trading systems or carbon taxes calculated on the basis of greenhouse gas emissions. The December 2025 amendment package does not fundamentally alter this architecture. However, the recitals accompanying the legislative proposal, together with the report on the application of the CBAM under Article 30(2) of the CBAM Regulation, signal that an implementing act specifying modalities for accounting for third-country carbon pricing is forthcoming:

“Under the planned implementing act setting rules for the deduction of a carbon price paid in a third country and its accompanying guidance, the European Commission will work on the principle of equivalence and will clarify how claims for carbon credits purchased under compliance schemes can be taken into account, including carbon credits under Article 6 of the Paris Agreement.”¹⁴

¹³ European Union, Regulation (EU) 2023/956 of the European Parliament and of the Council of 10 May 2023 Establishing a Carbon Border Adjustment Mechanism, 16 May 2023, <<https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32023R0956>>, Art. 9.

¹⁴ European Commission, ‘Report from the Commission to the European Parliament and the Council on the application of the Regulation on the Carbon Border Adjustment Mechanism’ COM(2025) 783 final, 16 December 2025, <<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:52025DC0783>>, at p. 18.

As noted during public information events and stakeholder consultations, this implementing act is expected later in Q1/2026 or early in Q2/2026.

So far, all legislative and policy documents have consistently stated that the carbon price has to be “effectively paid.” This signals a focus on actual price incidence at installation level, taking into account free allocation, rebates, exemptions, or other relief mechanisms. As evident from the cited passage of the report on the application of the CBAM above, the possible role of Article 6 credits under the Paris Agreement is being considered according to Recital 21 of the legislative proposal of December 2025 and background discussions, but without clarification of eligibility criteria or accounting safeguards:

“To facilitate the application of Regulation (EU) 2023/956, the Union may in the context of the Implementing Regulation for accounting the carbon price paid abroad, consider the carbon credits under Article 6 of the Paris Agreement.”¹⁵

Article 2(12) of the CBAM Regulation also provides a basis for bilateral agreements enabling the EU to take into account third-country carbon pricing mechanisms more structurally. To date, however, no implementing act has been adopted, and no formal bilateral recognition arrangements have been concluded.

2.4.2 ERCST assessment

The absence of operational guidance at the beginning of the definitive phase introduces uncertainty for importers and third-country policymakers alike. As reflected in the ERCST consultation informing this report, such uncertainty could blunt incentives for deployment of third-country carbon pricing and, by extension, investment in foreign decarbonisation. Accordingly, there is some urgency when it comes to issuing the implementing regulation operationalizing Article 9 of the CBAM Regulation, yet it must not only provide operational clarity but do so in a manner that is methodologically robust and attentive to the incentive effects and potential trade-offs it entails, as the resolution of the attendant accounting questions will simultaneously shape the credibility of the CBAM and the policy incentives it generates for carbon pricing and decarbonisation efforts abroad.

Methodologically, the central challenge lies in translating heterogeneous carbon pricing systems into an equivalent “effectively paid” carbon price embedded in imported goods. While the CBAM Regulation relies on the deduction of a carbon price “effectively paid” in the country of origin (Article 9), this concept does not eliminate the underlying comparability problem, but rather shifts it to a technically and legally complex *ex post* calculation. Emissions trading systems differ widely in scope, point of regulation, coverage thresholds, banking rules, offset use, and allocation design. In rate- or intensity-based systems, the carbon cost per tonne of output depends on performance benchmarks rather than an absolute cap, making the marginal carbon price faced by a producer analytically distinct from the nominal allowance price (Fischer et al., 2025). Similarly, free allocation, rebates, output-based updating, and carbon-price offsetting direct subsidy and compensation schemes reduce effective carbon cost incidence in ways that are not transparently observable. Determining the “effectively paid” amount therefore requires disentangling gross carbon liabilities from net fiscal transfers and indirect subsidies, raising difficult evidentiary and

¹⁵ European Commission. ‘Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EU) 2023/956 as Regards the Extension of Its Scope to Downstream Goods and Anti-Circumvention Measures’ COM(2025) 989 final, 17 December 2025, <<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52025PC0989>>, Recital 21.

attribution questions. Third, hybrid instruments (such as partial ETS coverage combined with command-and-control standards, energy taxes, or sectoral levies) complicate the boundary between explicit and implicit carbon pricing.

Even if the forthcoming implementing regulation adopts a restrictive approach limited to explicit pricing, exchange-rate effects, sectoral differentiation, and time-varying prices introduce additional volatility and measurement uncertainty. Verification of the carbon price paid poses non-trivial administrative burdens: assessing installation- and product-specific payments in third countries requires reliable, independently verified data. Recognizing the importance of verification, the proposed legislative amendment published in December 2025 would empower the European Commission to adopt:

“... implementing acts concerning the conditions to ascertain the qualifications of the person responsible for certifying, via the CBAM registry, the information contained in the carbon price documentation, and including the granting of an accreditation by a national accreditation body, and cover the necessary certification procedures and exchange of information.”¹⁶

In short, while reliance on the “price effectively paid” arguably represents the most tangible and objective metric to account for third-country climate policy efforts, it does not obviate methodological challenges, and presupposes a harmonised accounting framework capable of resolving them (Boute, 2024). Absent detailed implementing rules clarifying scope, netting rules, treatment of free allocation and rebates, and evidentiary standards, the concept risks masking unresolved comparability problems rather than solving them.

Beyond methodological challenges, the design of the implementing regulation will also have material incentive effects. As shown by previous research, the CBAM can serve as a motor for carbon pricing diffusion if foreign jurisdictions perceive a credible pathway towards recognition of their domestic carbon pricing systems (Mehling et al., 2025). Conversely, overly loose rules may discourage carbon pricing reforms and incentivise alternative policy instruments that fall outside Article 3(29). Recent proposals tabled in this debate have included options that would allow export taxes or non-carbon denominated levies (e.g. energy taxes) to qualify for crediting, or that would rely on project-based credits (e.g. Sandler and Schrag 2025). Such approaches have the benefit of increasing flexibility and ensuring that revenue remains with trade partner countries, but they also risk detaching the CBAM deduction from a broader, economy- or sector-wide explicit carbon pricing system. This, in turn, would weaken both environmental integrity and systemic coherence, potentially encouraging narrowly tailored instruments designed primarily to offset CBAM liability rather than to reduce emissions comprehensively.

Assessed against the criteria outlined in Section 2.1.3, the current state of the framework for recognising carbon prices paid in third countries thus raises several concerns.

- **Governance and legal implications:** The absence of an implementing act at the outset of the definitive phase creates a governance gap. Article 9 indicates a right to claim deductions, but the procedural and evidentiary conditions remain unspecified, generating legal uncertainty for importers and third-country governments alike. The announced consideration of Article 6 credits under the Paris Agreement adds further complexity, as

¹⁶ European Commission, n. 15 above, Recital 25.

their integration would need to be reconciled with both the accounting logic of Article 9 and the environmental integrity safeguards of the Paris Agreement, and carefully assessed for its incentive effects and the extent to which it mirrors the EU ETS which the CBAM adjusts for.

- **Political feasibility and external implications:** Third countries with explicit carbon pricing instruments will be closely attuned to whether the implementing regulation provides a credible recognition pathway. Overly restrictive criteria risk being perceived as dismissive of legitimate policy diversity, undermining climate diplomacy and the nationally determined architecture of international climate cooperation. Overly permissive criteria, by contrast, could attract domestic criticism from EU industry perceiving insufficient rigour as a competitive disadvantage.
- **Technical feasibility:** Translating heterogeneous foreign carbon pricing systems into a comparable “effectively paid” figure requires resolving methodological questions for which harmonised cross-jurisdictional approaches do not yet exist. Installation-specific payment data from third countries may be difficult to obtain and independently verify.
- **Environmental implications:** If the implementing regulation permits recognition of project-based credits or export-specific levies without anchoring these in a comprehensive domestic carbon pricing system, it risks weakening the CBAM’s environmental integrity and blunting the incentive effect to adopt carbon pricing policies abroad.
- **Competitive implications:** Generous recognition of foreign carbon pricing narrows the effective cost differential between EU and foreign producers; a stringent approach widens it. The treatment of free allocation and rebates in third countries is particularly consequential, as inconsistent netting rules could either overstate or understate the carbon costs actually borne by foreign producers.

2.4.3 Areas of alignment with ERCST analysis

The Commission’s insistence on “effectively paid” carbon prices aligns with ERCST’s past emphasis on avoiding double pricing while safeguarding environmental integrity (Marcu et al., 2023). The potential use of bilateral agreements under Article 2(12) is consistent with earlier calls for structured cooperation. However, alignment ultimately depends on implementation. ERCST analysis has consistently stressed predictability, transparency, and incentive compatibility. It has also highlighted concerns with an excessively generous approach to recognition of third-country carbon prices, for instance if it were to account for implicit carbon costs or export-only pricing; not only would this undermine the incentive effect for third countries to introduce or strengthen their domestic carbon prices, but it would also weaken the ability of the CBAM to level the average carbon costs facing producers within and outside the EU – and thus reduce carbon leakage – while potentially giving rise to a spiralling dynamic in which EU producers request the scope of the CBAM to be expanded to compliance costs beyond the EU ETS. The forthcoming implementing act will determine whether the CBAM stabilizes support for its current design and reinforces carbon pricing diffusion or whether it inadvertently weakens the suitability of the CBAM as a leakage safeguard and incentivises fragmented or strategically designed policy responses.

2.4.4 Looking forward

As argued above, the forthcoming implementing act on recognition of third-country carbon prices will have to navigate a set of technically and politically challenging trade-offs. Accordingly, the forthcoming implementing regulation should:

- articulate transparent eligibility criteria for recognised carbon pricing instruments;
- establish consistent methodologies for calculating “effectively paid” carbon prices;
- clarify treatment of free allocation, performance benchmarking, rebates, and hybrid instruments;
- define robust accounting standards for any recognised credits;
- provide legal certainty through clear procedural rules.

Crucially, the Commission should evaluate *ex ante* the incentive effects of alternative design choices. Recognition rules that are overly permissive could encourage narrowly scoped export levies or credit-based schemes designed primarily to offset CBAM liability. Conversely, overly restrictive rules could dampen incentives for comprehensive carbon pricing reform.

ERCST recommends maintaining the core logic of Article 9: crediting should remain anchored in an explicit domestic carbon pricing system. Flexibilities – such as additional allowance purchases or tax payments, foregoing of rebates and free allocation, or compliance credits – may be recognised, provided they are demonstrably embedded within, and accounted for under, the domestic carbon pricing system. Ultimately, however, all such options further increase the complexity of the CBAM, so that bilateral agreements concluded under Article 2(12) of the CBAM Regulation may offer a more pragmatic and administratively feasible approach to contending with the idiosyncrasies and heterogeneous particularities of carbon pricing regimes in third countries. Hence, offering clarification of the exact purpose, scope and procedural implications of these agreements is another important policy recommendation.

2.5 Exports of Goods

2.5.1 Commission measures

Export-related leakage remains a distinct channel of carbon leakage. As documented in Marcu et al. (2024), exporters may face loss of market share in jurisdictions without equivalent carbon constraints as free allocation declines and the CBAM only levels the playing field for imported goods. The Commission has proposed a Temporary Decarbonisation Fund (TDF) to address this problem: on 17 December 2025, the Commission published a legislative proposal establishing the TDF, conceived as a time-limited response to the heightened risk of carbon leakage as free allocation under the EU ETS is phased out concurrent with CBAM phase-in. The fund is designed as a bridge solution, pending a more comprehensive treatment in the context of the EU ETS revision expected in mid-2026.

More specifically, the TDF would be financed from 25% of Member State revenues from the sale of CBAM certificates for embedded emissions declared for 2026 and 2027, with estimated resources of approximately €633 million (European Parliament, 2026). A single call for applications would be launched in 2028, with support disbursed to eligible operators by end-2029. Eligibility is limited to operators producing goods listed in an annex, covering approximately 25% of all CBAM-covered products in the aluminium, fertilisers, and iron and steel sectors. Electricity, cement, and hydrogen are excluded. Member States may request inclusion of additional goods with low value-to-weight ratios and heightened national-level carbon leakage risk. Notably, there is no proof-of-export requirement: support is allocated on the basis of production, irrespective of whether goods were subsequently exported. To receive support, operators must satisfy conditionality requirements linked to decarbonisation, including implementation of energy audit

recommendations, demonstration that any recommendations not yet implemented have payback periods exceeding five years, or legal investment commitments towards equivalent emissions reductions or climate neutrality plan targets.

2.5.2 ERCST assessment

The principal concern with the Fund is lack of specificity. If eligibility extends broadly across producers within a sector, limited resources risk being distributed too thinly to meaningfully offset carbon cost asymmetries faced by exporters. Absent a link to export exposure, support may fail to reach those installations most vulnerable to relocation or investment diversion due to loss of global market share and export-related leakage.

Assessed against the criteria set out in Section 2.1.3, the TDF raises a number of concerns alongside its merits.

- **Governance and legal implications:** Key operational details – including opt-in eligibility, application procedures, and monitoring – are left to delegated and implementing acts, concentrating significant discretionary power in the Commission. At the international level, using CBAM revenue to support EU producers may attract scrutiny under WTO subsidy rules. Whether the fund’s decarbonisation conditionality sufficiently distinguishes it from a prohibited or actionable subsidy will depend in part on the deliberate absence of an explicit export link, but also on how the measure is perceived in practice.
- **Political feasibility and external implications:** The fund responds to longstanding industry demands. However, initial reactions have been mixed: industry associations have criticised the limited scope and temporary nature, while environmental organisations warn that it risks undermining carbon pricing integrity by compensating emitters. Internationally, the use of CBAM revenue to support domestic producers may be perceived as protectionist.
- **Technical feasibility:** The design draws on existing EU ETS reporting infrastructure and a single call for applications. However, challenges may arise in the assessment of conditionality requirements, particularly where operators rely on climate neutrality plans or alternative equivalent measures.
- **Environmental implications:** Where conditionality functions effectively, the fund could accelerate decarbonisation in trade-exposed sectors. However, pursuant to Article 7(1)(b), where operators demonstrate payback periods exceeding five years, no additional conditionality applies, nor is there a requirement that support be channelled towards further decarbonisation effort. Further, the absence of a proof-of-export requirement means resources may flow to operators whose production is predominantly sold on the internal market, where the CBAM already provides protection.
- **Competitive implications:** The TDF responds to growing cost asymmetries for EU exporters as free allocation declines. However, estimated eligible demand of approximately €265 million is modest relative to total phased-out free allowances over 2026–2027 (approximately €1.5 billion, cf. European Parliament, 2026). The absence of a link to export exposure directs resources on the basis of production volumes rather than trade intensity, potentially missing operators most exposed to global competition.

2.5.3 Areas of alignment with ERCST analysis

ERCST's earlier work on this topic has proposed an alternative, more targeted approach: export certificates (Marcu et al., 2022; Marcu et al., 2024; Marcu et al., 2025). Under this model, exporters would receive certificates corresponding to the carbon costs embedded in exported goods, up to a benchmark level aligned with ETS free allocation rules. Certificates would not be tradable on the secondary market, but would be redeemable towards compliance with the EU ETS to lower the carbon costs facing exporters. The mechanism would:

- maintain symmetry with ETS benchmarks;
- preserve the domestic carbon price signal;
- avoid direct export rebates at the border;
- link compensation directly to exported volumes;
- remain administratively tractable by building on existing ETS data infrastructure.

This approach was designed to balance WTO considerations with environmental integrity and competitiveness objectives. While legal concerns regarding export-linked compensation are not trivial, the alternative – broad, thinly spread financial support – risks insufficiently addressing carbon leakage in trade-exposed sectors. In a context of constrained fiscal space, prioritization becomes unavoidable. Ensuring the resilience, competitiveness, and long-term prosperity of EU industry in a decarbonizing global economy may warrant carefully calibrated, export-sensitive mechanisms.

The Commission's preference for a decarbonisation-linked instrument reflects ERCST's emphasis on maintaining environmental integrity and avoiding blunt export rebates. However, the absence of a structured link to export exposure diverges from ERCST's earlier recommendations. The export certificate proposal remains consistent with the CBAM's broader objectives, provided it is benchmark-based, proportionate, and transparent.

2.5.4 Looking forward

As ETS reform advances, a durable export solution should:

- reflect the free allocation phase-out trajectory;
- seek to be revenue-neutral to avoid being limited by budgetary constraints;
- maintain decarbonisation incentives;
- provide medium-term predictability to guide investment decisions;
- and, most importantly, be explicitly linked to export exposure so it can effectively mitigate the risk of export-related leakage.

The Temporary Decarbonisation Fund may serve as a bridge, but cannot substitute for a long-term structural solution. Such a refined export certificate mechanism therefore merits renewed consideration in the context of the post-2030 ETS architecture.

2.6 Downstream Extension

2.6.1 Commission Measures

Summary of legal changes introduced

- Extension of CBAM coverage downstream in the aluminium and steel sectors, covering 180 additional goods, or roughly an additional 15% of covered goods.
- To be clear: coverage would mean requiring CBAM certificates only for the embedded emissions in such goods that would have been covered by the ETS had the good been manufactured in the EU. This means, for example, that if the downstream processor would not be covered under the EU ETS then no CBAM certificates would be due for emissions created during the production of the newly covered good itself – only for the emissions embedded in the CBAM-covered inputs to that production.¹⁷

Key objectives stated by the Commission

The objective of the proposed downstream extension is to “address the risk of carbon leakage for products further down the value chain of the steel and aluminium products currently in CBAM’s scope.”¹⁸

The idea is that wherever in the value chain CBAM coverage stops, there is risk that foreign producers that might have previously exported goods within that stopping point will simply process goods to a point just beyond it, to avoid incurring CBAM liabilities. In that scenario, if the cost of carbon as a share of final price were high enough for the goods in question, the foreign producers would gain a competitive advantage over EU producers. The result would be lost market share and carbon leakage.

New tools, powers, or definitions introduced

Under the proposed extension, all existing regulatory tools and powers would continue as before, now applicable to the newly covered sectors.

Enforcement and monitoring mechanisms envisaged

The Commission already has in place a mechanism to monitor the impact of the CBAM on carbon leakage, which would presumably include an assessment of its effectiveness at preventing leakage downstream of covered goods. Before January 2028, and every two years thereafter, the Commission is obliged to present a report on this and other matters to the European Parliament and Council.¹⁹

While the proposal for a regulation itself does not list any additional monitoring functions related to downstream extension, the impact assessment describes a monitoring effort that would presumably be implemented in the context of the above-mentioned regular report:

¹⁷ This principle, which ensures that the CBAM mirrors the ETS in its treatment of foreign goods, was enunciated for all downstream goods in the CBAM simplification regulation adopted in October 2025: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L_202502083.

¹⁸ European Commission. (2025). “Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2023/956 as regards the extension of its scope to downstream goods and anti-circumvention measures” COM(2025) 989 final, p. 1.

¹⁹ European Union. (2023). “Regulation (EU) 2023/956 of the European Parliament and of the Council of 10 May 2023 Establishing a Carbon Border Adjustment Mechanism.” L 130/52. Article 30(6).

“Monitoring will ... track the average emission intensity of imported goods, the total level of emissions at sectoral level for imported and EU produced products covered by the [downstream] extension, changes in their import and export levels, [and] the share of declarations relying on default values versus actual emissions reporting ...”²⁰

2.6.2 ERCST assessment

- **Governance and legal implications:** The proposal has the potential to raise legal concerns with the CBAM regime. This would be the case if the newly covered sectors were not in fact at significant risk of leakage, and the extension ended up protecting the competitiveness of downstream producers but not preventing much in the way of leakage-related GHG emissions. The WTO-legal acceptability of the CBAM, by most legal opinion, rests on its ability to cast itself as an environmental measure eligible for carve-outs to the GATT rules under GATT’s Article XX exceptions. But those exceptions are designed to filter out any measures nominally aimed at environmental protection which in fact protect competitiveness.
- **Political feasibility / implications:** Domestically, the proposal for extension is politically feasible. It would result in insignificant cost increases for domestic consumers in the covered goods²¹, and would be welcomed by the newly-covered downstream producers. It might not be as welcome for processors downstream of the newly-covered goods, for whom input prices would increase.

On the other hand, the proposal would increase the burden of compliance on foreign producers of the newly covered goods and their associated importers. They would face the prospect of soliciting emissions data much further up the value chain, or using default values that might be punitive, in part because of the mandated use of mark-ups. The more prior stages of production for which importers have to provide data, the more challenging it becomes to report actual data.

In an effort to address this challenge, the proposal moots special treatment for complex downstream goods produced with multiple CBAM-covered precursors, where those inputs are from different sectors or non-CBAM-covered sectors.²² For such goods, it is proposed that the use of default values should be facilitated by not applying the mark-up that is applied to other CBAM goods’ default values, “without prejudice to the environmental integrity of the CBAM”. Presumably at least some of the newly-covered downstream goods would qualify for such treatment, but the proposal does not actually specify which goods might be eligible, or explain what restrictions to that list might be implied by the caveat about environmental integrity. The proposed legal changes to the regulation simply note

²⁰ European Commission. (2025). “Impact Assessment Report Accompanying the Document ‘Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2023/956 as regards the extension of its scope to downstream goods and anti-circumvention measures.’” SWD(2025) 988 final, Part 1. P. 59.

²¹ The most heavily affected final goods impacts are for the construction sector, which would see a minor estimated cost increase of 0.12%. *Ibid.* Section 6.2.4.1.

²² European Commission. (2025). “Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2023/956 as regards the extension of its scope to downstream goods and anti-circumvention measures” COM(2025) 989 final. P. 16

that the Commission “may provide a list of downstream goods” eligible for such treatment in implementing acts.²³

- **Technical feasibility:** The proposal would increase the number of CBAM-covered importers by an estimated 7,000 – 7,100, and would require that they either solicit emissions data far up the value chain, or resort to the use of default values for embedded emissions. For many of those importers, the latter option would likely be infeasible.

An increase of that magnitude risks proportionately increasing the burden associated with administering the CBAM, and complying with it. For that reason, the impact assessment assessed the options for coverage against two efficiency indicators—EU production emissions per additional CN code, and import emissions per additional importer covered—and a proportionality indicator: the share of additional CN codes with more than 70% basic CBAM materials by weight. The former tries to balance the scale of emissions covered against the complexity and cost of adding more CN codes and implicating more importers. The latter assumes that it will be administratively easier to cover goods with a high share of basic material by weight.

- **Environmental implications:** The proposed extension is estimated to reduce carbon leakage in the downstream sectors by more than half by 2035, from 63% to 26%.²⁴ While this is a significant reduction in percentage terms, the extension of downstream coverage is relatively insignificant in terms of absolute global environmental impact, representing less than a single megatonne (0.83) of global CO₂e emission reductions. In pursuit of the objective of leakage prevention, the choice of goods to include in the proposed expansion was made using two filters (the parameters for which were determined by considering the indicators discussed above):²⁵
 1. “Carbon leakage filter”: a standard two-pronged threshold for leakage risk, involving fulfilling two conditions: carbon cost of more than 5% of gross value added, and trade intensity of more than 10%. This is a similar formulation to the test the EU uses to determine risk of leakage under the EU ETS.
 2. “EU production emission floor”: a minimum threshold test for the total amount of emissions embodied in the annual EU consumption of the good in question, looking just at the emissions attributable to the basic goods (cement, aluminium, steel) they contain. The threshold is set at 150,000 tonnes of CO₂e.
- **Competitive implications:** Relative to the baseline case of continuing with existing CBAM coverage, the proposed downstream extension has positive—but minimal—impacts on the output of the covered goods. The most favourably impacted sector is

²³ *Ibid.* Amendment 6(c), p. 23.

²⁴ European Commission. (2025). “Impact Assessment Report Accompanying the Document ‘Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2023/956 as regards the extension of its scope to downstream goods and anti-circumvention measures.’” SWD(2025) 988 final, Part 1, Section 6.2.2.2.

²⁵ European Commission. (2025). “Impact Assessment Report Accompanying the Document ‘Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2023/956 as regards the extension of its scope to downstream goods and anti-circumvention measures.’” SWD(2025) 988 final, Part 2 (Annexes), Annex 4.

“fabricated metal products,” where the extension is estimated to increase output by 2035 by 0.16% relative to the baseline.²⁶

In a similar vein, extending coverage downstream is estimated to reduce imports of the newly-covered goods relative to the baseline in which those goods were not covered. This is positive, but the actual increment of protection is very small; imports are estimated to decrease by only 0.29% by 2035.

The loss of competitiveness in the EU exports of the newly-covered goods is similarly very minor. The proposed downstream extension would raise the price of inputs for those processors further down the value chain from the newly covered goods, but those price increases are likely to be only slightly more significant than the small estimated increases in prices in final goods.

2.6.3 Areas of alignment with ERCST analysis

ERCST has recommended that in considering downstream expansion the EU should employ the same tests that it used to decide which sectors/goods should be included in CBAM coverage under the original regulation.²⁷ The two filters described broadly correspond to two of the criteria used in that context. The CBAM impact assessment described these two criteria as:²⁸

- The sector’s exposure to significant risk of carbon leakage; and
- Whether the sector is one of the largest aggregate emitters of GHG emissions.

The original choice had a third criterion, that roughly corresponds to the efficiency and proportionality indicators used to decide what parameters to assign to the criteria above:

- Balancing broad coverage in terms of GHG emissions while limiting complexity and administrative effort.

Achieving that balance is clearly a subjective call, but the obvious question is whether, given the administrative burden and complexity involved in adding 180 products and involving 7,000 or more new declarants, relative to the meagre additional benefits in terms of GHGs reduced, this balance is adequately reflected in the Commission proposal. It is worth noting that even if declarants choose to use default values to avoid complexity, and even if mark-ups are not assessed on those values (not certain at this point), downstream extension involves two types of new costs for the 7,000 or more declarants that are implicated:

- The cost of basic reporting; and

²⁶ European Commission. (2025). “Impact Assessment Report Accompanying the Document ‘Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2023/956 as regards the extension of its scope to downstream goods and anti-circumvention measures.’” SWD(2025) 988 final, Part 1, Section 6.2.3.2.

²⁷ Marcu et al. (2025). “Extension of the CBAM Scope.” ERCST. <https://ercst.org/extension-of-the-cbam-scope/>

²⁸ European Commission. (2021). “Impact Assessment Report Accompanying the Document ‘Proposal for a Regulation of the European Parliament and the Council Establishing a Carbon Border Adjustment Mechanism.’” SWD(2021) 643 final. Section 5.2.1.3., p. 21.

- The cost of CBAM liability; basic default values are costly to some producers, whose actual emissions intensity they may significantly overstate.

2.6.4 Looking forward

- **Upcoming implementing acts or guidance**

The proposal does not envision any new acts or guidance.

- **Review clauses or future legislative steps**

As noted above, there is a commitment to monitor trade flows, the use of actual and default data, and emissions intensity in the newly-covered downstream goods, with a view to gauging the impacts of the extension on the CBAM's objective of reducing carbon leakage. This will probably take place in the context of the reporting mandated in Regulation Article 30. The first of these reports is due before January 2028, with regular reports every two years thereafter.

- **Recommendations**

The Commission has considered a number of issues that have been raised by stakeholders, in deciding the scope of its proposed extension, accounting for risk of leakage, aggregate GHG emissions involved, proportionality, and efficiency.

But the final result seems to involve more complexity/compliance cost, administrative burden than is easily justified by the results in terms of avoided risk of carbon leakage, trade and output impacts, and GHG emissions avoided. For context, recall that the further down the value chain we go, the less risk of leakage and competitiveness impacts exists:

- The more processed is a good, the more embedded carbon cost shrinks as a share of gross value added and final price.
- The pass-through of carbon costs is never 100% at any stage of the value chain.
- The more processed a good is, the more non-price factors (branding, reliability, etc.) become important in buying decisions.

As such, the Commission should pursue a more limited set of goods for downstream coverage, such as for example the “option 1” case that was considered in the impact assessment, covering only 70-80 CN codes of goods with highest risk of carbon leakage and significant climate relevance, and implicating only 1,400-1,500 new importers. Granted, the result would be more carbon leakage as compared to the “option 2” case that the Commission recommends, but the absolute levels of trade and climate impacts involved would be minor. The difference between the two options is roughly half a Mt of CO₂e of global CO₂e emissions, and at most a tenth of a percent of sectoral output by 2035.

Beyond the concerns about complexity and compliance cost, if the proposed extension included goods for which the actual risk of leakage is relatively low, then the credibility and legality of the CBAM regime would be undermined.

3. Conclusion

The December 2025 legislative proposals represent an important step in the operationalisation of the Carbon Border Adjustment Mechanism as it moves from the transitional period into its definitive phase. It puts forward means to address several issues that have been central to the CBAM debate in recent years, and in this regard it is welcome. At the same time many critical issues remain unaddressed or are still waiting for a permanent solution.

Overall, the proposals show an effort by the Commission to make the mechanism fit-for-purpose and to address risks that could undermine its objectives. On anti-circumvention, measures aimed at reducing mis-declaration of emissions and improving monitoring along supply chains should have positive results in some circumstances, by addressing the treatment of pre-consumer scrap, the disaggregation of CN codes, and requiring additional evidence in cases of high risk. The lack of coverage for post-consumer scrap is a significant gap in protection against leakage and competitiveness impacts.

But those measures fall short of providing solutions to some of the more fundamental avoidance challenges facing the mechanism. In particular, the broader provisions on abusive practices remain insufficiently defined, and their practical application will need to avoid constraining normal market responses to carbon pricing signals, including investments in lower-emission production destined for export to the EU.

The introduction of Article 27a adds a safeguard mechanism that allows temporary exclusions from CBAM coverage in cases where severe disruptions linked to price developments affect the internal market. While such flexibility may prove useful in exceptional circumstances, the interpretation of the legal thresholds, such as “severe harm” and “serious and unforeseen circumstances”, will need to be clearly defined in order to preserve regulatory predictability.

At the same time, several elements of the package raise questions that will need to be resolved during implementation. The forthcoming implementing act on recognising carbon prices paid in third countries under Article 9 will be particularly important. Its design will determine whether the CBAM creates incentives for the adoption of explicit carbon pricing abroad or instead encourages narrowly tailored instruments aimed primarily at offsetting CBAM liability. Beyond the individual deduction mechanism, there also needs to be a better understanding of how the bilateral agreement pathway provided for under Article 2(12) of the CBAM Regulation would operate in practice, including what conditions partner countries would need to meet, and what the implications of such arrangements would be for the overall coherence of the CBAM framework.

The Commission has adopted a structured approach to downstream extension, filtering goods by carbon leakage risk and aggregate emissions relevance, criteria broadly consistent with those used to determine the original CBAM scope. However, the resulting proposal covers 180 additional goods and implicates over 7,000 new importers, while the estimated global emission reductions amount to less than one megatonne of CO_{2e}. A more targeted scope, such as the narrower option considered in the impact assessment covering 70–80 CN codes and approximately 1,400–1,500 importers, could achieve a more defensible balance between administrative burden and avoiding risk of leakage. There is also the issue of how far downstream the CBAM is going to have to go, the fact that it becomes impractical at some point as well as a general philosophical question of where the regulatory intervention should stop.

Finally, export-related leakage remains a major unresolved structural issue. The Temporary Decarbonisation Fund is a shotgun approach solution – its lack of a direct link to export exposure limits its effectiveness in addressing carbon cost asymmetries faced by EU producers on global markets. As free allocation under the EU ETS is phased out, a more targeted mechanism, such as the export certificate approach proposed by ERCST, linking compensation to the carbon costs embedded in exported goods, will likely be required to durably address this channel of leakage.

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