

CBAM for the EU – Redline issues

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Roundtable on
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Sustainable Transition

Introduction: Our Approach

- Our previous work has **unpacked CBAM design elements** and implementation options, highlighting the **complexity** of this instrument and the **trade-offs** of alternative designs.
- The **political debate** on CBAM – as an integral part of the “Fit for 55” package under the European Green Deal – has revealed **heterogeneous preferences** among key stakeholders.
- Building on a **multi-criteria analysis** and extensive **consultations** with stakeholders in the EU and abroad, the latest ERCST report proposes a **CBAM design** that **balances tradeoffs** and remains **technically, legally and politically viable**.

Methodology

Eight design elements:

- Coverage of trade flows
- Policy mechanism
- Geographic scope
- Sector/product scope
- Emissions scope
- Determination of embedded emissions
- Calculation of adjustment
- Use of revenue

Five evaluative criteria

- Environmental benefit
- Competitiveness benefit
- Technical and administrative feasibility
- Legal feasibility
- Political and diplomatic feasibility

Guiding Principles & General Assumptions (I)

- **Objectives: A menu**
 - Avoid carbon leakage
 - Address competitive concerns
 - Allow for increase EU level of ambition
 - Motivate trade partners
 - Eliminate free allocation
 - Generate revenue
 - **ERCST:** address risk of carbon leakage by addressing competitive concerns resulting from the costs of climate action, in domestic and international markets
- **WTO compliance**
 - Interpretations of what is and what is not aligned with WTO may change in the future.
- **Compliance**
 - Compliance obligation will be on importers

Guiding Principles & General Assumptions (II)

- **No double protection**
 - Domestic producers cannot end up being better off than foreign producers
 - Application should not be driven by ideology.
- **Operationalization**
 - CBAM will require a significant level of administrative effort
 - EU and/or international institutional changes, new structures may need to be created.
- **CBAM & EU ETS**
 - It is thus a companion policy to the EU ETS
 - CBAM will impact the functioning of the EU ETS
- **Pilot phase**
 - May differ from what the final design of a CBAM may be.
 - Allows for gradual and cautious introduction of approaches that need to be tested.
 - Covers 2023-2027, takes into account the Paris Agreement stocktake

Redline issues

- Essentially it is an opportunity to look at these, and possibly other issues, and discuss:
 - what issues are critical
 - can they be addressed in the current context
 - how can they be addressed as options
 - other questions

Redline issues

- **Indirect emissions and costs:** inclusion of scope 2 & 3 emissions, value chain coverage threshold
- **Exports & Free allocation** (coexistence issue, exports application)
- **Accommodating foreign climate action:** allowing challenges of the default, and including national exemptions

Indirect emissions and costs

Determining the carbon intensity of imports can be based on Scope 1 emissions only, or also reflect Scope 2 (and even Scope 3) emissions

- Include Scope 2 emissions from off-site electricity/heat/steam?

Yes: EU producers face pass through of carbon price on electricity/heat

No: Would disadvantage EU producers - carbon cost pass-through not linked to Scope 2 emissions, but result of price formation in wholesale electricity market; resource shuffling

- Include Scope 3 emissions from: a) raw material inputs? b) transport?

Yes: a) Many vulnerable products further downstream, their carbon intensity (e.g. extruded products) linked to raw material input b) transport emissions matter for climate, some transport already covered by EU ETS, otherwise by other rules, EU ETS coverage may expand

No: a) adds administrative complexity, any threshold arbitrary, merely shifts leakage downstream b) CBAM complements ETS, currently shipping, road transport not included

Exports and free allocation

- Red lines:
 - No free allocation abruptly
 - No provision for exports
- Maintain decreasing free allocation
- CBAM for what is not covered by free allocation
 - Will allow for a phasing out process for free allocation
 - Allows to test CBAM
 - Will address exports that cannot be otherwise addressed under WTO
 - Need to avoid double protection
 - Depending on design may allow increased protection from current situation

Accomodating foreign climate action

Three tracks, two red lines:

- Allow challenges of any default GHG intensity assumptions
 - Compelled by legal and political realities, but creates risk of resource shuffling
- Credit for carbon price paid in exporting country
 - Practically required, but not a red-line issue
- Exempt countries on the basis of their policies
 - Compelled by political realities, but a minefield of legal, environmental, political, methodological challenges

Thank you

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