

Regulatory Alert

Global Environmental and Chemical Regulations, Policies, and Standards

Alert 31



Carbon Border Adjustment Mechanism Region: Europe

WHY IS THIS ALERT IMPORTANT?

If your company imports certain carbon-intensive¹ goods originating in a country or territory outside the customs territory of the European Union (EU) into the EU, you are legally obligated to comply with the [Carbon Border Adjustment Mechanism](#) (CBAM), established by the [Regulation \(EU\) 2023/956](#) (the Regulation) that was published on 16 May 2023 and entered into force on 17 May 2023. Certain articles of the CBAM were in force as early as 1 October 2023.

With the introduction of CBAM, certain carbon-intensive goods entering the EU are subject to a price based on the amount of carbon emitted during production. The EU CBAM Regulation aims to prevent the risk of carbon leakage² from non-EU-produced goods and to encourage cleaner industrial production in non-EU countries that do not have equivalent climate policies. Certain articles of the CBAM started to be applied on 1 October 2023 with the rest phased in gradually, as detailed in Article 36 of the Regulation, with a transition period where the obligation of the importer is limited to reporting. The full measures of CBAM will be implemented on 1 January 2026.

Penalties for non-compliance to the CBAM Regulation shall be imposed by the Member States and may include fines, as mentioned in Article 26 of the Regulation. CBAM needs to be reviewed in addition to [EU customs code](#) to analyse the impact.

INTENDED AUDIENCE

This Regulatory Alert is intended for IAEG members and their suppliers who manufacture or import carbon-intensive goods covered by the CBAM Regulation into the EU.

EXECUTIVE SUMMARY

CBAM is a measure that puts a carbon border tariff on the carbon emitted during the production of certain carbon-intensive goods (listed in Annex I to the Regulation) originating in a third country³ when imported into the customs territory of the EU. However, third countries and territories outlined in Annex III to the Regulation are exempted from the scope. Additionally, CBAM applies to products held offshore but within the ocean territory of a Member State. The CBAM also extends to processed items that are derived from goods

¹ Carbon intensity is the amount of carbon dioxide and other greenhouse gases (CO₂e) produced per unit of activity, like the amount emitted during the production of a particular product. For example, electricity generated using fossil fuels (such as petroleum, coal, etc.) is carbon intensive.

² Carbon leakage refers to a situation where a company decides to move their production from a country with stringent climate policies, to a country with laxer emission constraints, leading to an increase in greenhouse gas emissions.

³ A third country is a country or territory outside the customs territory of the EU.

manufactured through the inward processing procedure mentioned in Article 256 of [Regulation \(EU\) No 952/2013](#), even where the processed products are not goods listed in Annex I to this Regulation. These items are subject to CBAM when they are imported into the EU's customs territory or held offshore within a Member State's ocean territory.

The CBAM aims to prevent carbon leakage if consumers buy goods that are substitutes for goods produced in the EU, from non-EU countries that levy a lower carbon price (or no carbon price), or if companies switch production activities from the EU to such countries to take advantage of the lax standards. The covered goods are those most at risk of carbon leakage and include, but are not limited to, iron and steel, aluminum, hydrogen, and electricity.

BACKGROUND ON REGULATION

As part of the [European Green Deal](#), the EU plans by 2030 to reduce greenhouse gas (GHG) emissions by at least 55% compared to 1990 levels and aims to become climate-neutral by 2050. However, some non-EU countries still implement weaker environmental and climate policies. Thus, carbon-intensive EU-based businesses could, for example, shift production abroad to take advantage of lax standards or import more carbon-intensive products to replace the EU products. As a result, emissions can be shifted outside of Europe, seriously undermining EU and global climate efforts. Hence, the CBAM was introduced to support the GHG emissions reduction goal by preventing the risk of carbon leakage from imported products and making sure that the carbon price of imports is equivalent to the carbon price of domestic production.

The CBAM phases out the free allowances established under [Directive 2003/87/EC](#) (the Directive) and mirrors the [EU Emission Trading System \(ETS\)](#) already implemented within the Union under the Directive. The EU ETS is a cornerstone of the EU's policy to combat climate change and its key tool for reducing greenhouse gas emissions cost-effectively. It is the world's first major carbon market and remains the biggest one. It sets a cap on the total amount of certain greenhouse gases that can be emitted from industries to encourage emission reductions and promote investment in innovative, low-carbon technologies. It allows emission allowances to be bought by industries but is limited, to maintain value, thereby preventing carbon leakage.

The working principle of CBAM

The EU international policies and commitments, including World Trade Organization (WTO) rules, have been incorporated into the CBAM to comply with EU international obligations. CBAM mirrors the EU ETS as summarised below.

- » A formula (see Annex IV to the Regulation) reflecting the effect of the EU ETS on similar EU-produced goods will be used to apply the CBAM to the actual declared carbon content embedded in the goods imported into the EU.
- » Covered goods can only be imported into the EU by an authorized CBAM declarant⁴ who purchases CBAM certificates⁵ equivalent to the carbon price required had the goods been produced under EU carbon pricing.

⁴ An authorized CBAM declarant is a person authorized by a competent authority in accordance with Article 17 of the Regulation.

⁵ A CBAM certificate is a certificate in an electronic format corresponding to one tonne of CO₂e (carbon dioxide equivalent) of embedded emissions in goods.

- » The CBAM helps reduce carbon leakage risk while encouraging producers outside the EU to adopt environmentally friendly production methods and countries to introduce carbon pricing measures.

Emission coverage

The two types of emission coverage mentioned in the CBAM Regulation are *direct emissions* and *indirect emissions*. Direct emissions are emissions from the production processes of covered goods, including emissions from the production of heating and cooling that is consumed during the production processes, irrespective of the location of the production of the heating or cooling. Indirect emissions are emissions from the production of electricity that is consumed during the production processes of covered goods, irrespective of the location of the production of the consumed electricity – under the CBAM indirect emissions are analysed before they are included in future products.

Embedded emissions in goods are to be calculated as specified in Annex IV to the Regulation. Embedded emissions mean direct emissions released during the production of goods and indirect emissions from the production of electricity consumed during the production processes. Therefore, only direct emissions are to be calculated and considered for goods (iron and steel, aluminium, and hydrogen) listed in Annex II to the Regulation.

APPLICABILITY

The CBAM initially applies to the imports of goods listed in Annex I to the Regulation from all third countries and territories other than those listed in Annex III to the Regulation. The covered goods⁶ have been explicitly selected because they pose an elevated risk of carbon leakage and possess high emission intensity that will eventually represent over 50% of the emissions (when fully phased in) in ETS-covered industry sectors. The key greenhouse gases covered by the CBAM Regulation are carbon dioxide (CO₂), and perfluorocarbons (PFCs) for some aluminium goods.

As specified in Annex III to the Regulation, the following third countries and territories are outside the scope of the Regulation: Iceland, Liechtenstein, Norway, Switzerland, Büsingen, Heligoland, Livigno, Ceuta, and Melilla.

RELEVANT DATES

The following dates apply to all Member States:

- » 1 October 2023 - 31 December 2025: Transitional period – Application [Article 33 (importation of goods); Article 34 (reporting obligation for certain customs procedures); and Article 35 (reporting obligation)] – first reporting period for importer ending 31 January 2024
- » 31 December 2024: Application [Article 5 (application for authorization); Article 10 (registration of operators and of installations in third countries); Article 14 (CBAM registry); Article 16 (accounts in the CBAM registry); and Article 17 (authorization)]
- » 1 January 2026: Application [Article 2(2) and Articles 4, 6 to 9, 15 and 19, Article 20(1), (3), (4) and (5), Articles 21 to 27 and 31]
- » 1 January 2026: The CBAM to be fully implemented

⁶ Covered goods include but are not limited to iron and steel, aluminium, hydrogen, and electricity (identified by their Combined Nomenclature ('CN') codes under Regulation (EEC) No. 2658/87.

The transitional period aims to collect useful information on embedded emissions to refine the methodology for full implementation of the CBAM. Rules and requirements for the reporting of emissions will be further specified in an implementing act to be adopted by the European Commission.

REGULATORY OBLIGATIONS AND EXEMPTIONS

- » Prior to importing the mentioned carbon-intensive goods into the customs territory of the EU, an importer established in a Member State, or an indirect customs representative⁷ in accordance with Article 18 of [Regulation \(EU\) No 952/2013](#), must apply for the status of authorized CBAM declarant via the CBAM registry under Article 14.
- » By 31 May each year (for the first time in 2027 for the year 2026), the authorized CBAM declarant must submit a CBAM declaration for the preceding calendar year via the CBAM registry, which will include the total quantity of each type of goods imported, their total embedded emissions, the total number of CBAM certificates to be surrendered, and copies of verification reports issued by accredited verifiers. The price of the CBAM certificates will be calculated depending on the weekly average auction price of EU ETS allowances expressed in €/tonne of CO₂ emitted.
- » The carbon price paid by non-EU producers on embedded emissions to produce imported goods can be fully deducted by importer from the CBAM obligation if the carbon price has already been paid in a third country. Necessary records must be declared to claim such deductions and must be kept until the end of the fourth year after the year during which the CBAM declaration has been or should have been submitted.
- » The obligations of the importer under this Regulation are limited to the reporting obligations set out in Articles 33 (importation of goods), 34 (reporting obligation for certain customs procedures), and 35 (reporting obligation) during the transitional period (1 October 2023 - 31 December 2025).
- » Reporting obligations of the importer do not apply to:
 - Processed products from outward processing procedure – this refers to goods temporarily exported from the EU for processing and then re-imported (detailed in Article 259 of Regulation (EU) No 952/2013).
 - Goods qualifying as returned goods – this refers to goods re-imported into the EU in the condition in which they were exported (i.e., unaltered) within three years of their export from the EU (detailed in Article 203 of Regulation (EU) No 952/2013).

RISKS TO AEROSPACE AND DEFENSE

- » Penalties for non-compliance to the CBAM shall be imposed by the Member States and may include fines, as mentioned in Article 26 of the Regulation.

⁷ An indirect customs representative is a person established within the customs territory of the Union in which case the customs representative shall act in his or her own name but on behalf of another person.

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- » Industry will have difficulty in obtaining a relevant and auditable carbon assessment for the raw materials/energy procured.
- » There is a potential impact on costs for the aerospace products that require an extensive use of such materials/energy in their production process.
- » CBAM needs to be reviewed in addition to EU customs code to analyse the impact.

USEFUL LINKS

[Regulation \(EU\) 2023/956 of the European Parliament and of the Council of 10 May 2023 establishing a carbon border adjustment mechanism](#)

[Carbon Border Adjustment Mechanism](#)

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