

## **CBAM: Nowhere close to the economic and environmental objectives**

**This June the European Parliament will vote on the Carbon Border Adjustment Mechanism (CBAM) proposal. The European Parliament and the Council still have an opportunity to reassess CBAM and ensure that its objectives can be fulfilled. As it stands, CBAM will fall short of its objective, and drive production and investment outside of Europe incentivising the relocation of factories outside the EU.**

### **(Illustration)**

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Putting a price on carbon is not an easy task. Over the past two decades, Europe has become a world leader in carbon pricing policies with the development of its Emissions Trading System (EU-ETS), the first and largest binding carbon market ever made. For sectors considered to be “at risk of carbon leakage”, a system of free allowances was introduced to keep jobs and investments in Europe. In the absence of any better solution, installations strongly exposed to international competition received hundreds of thousands of free carbon allowances since 2005.

The Commission’s proposal for a Carbon Border Adjustment Mechanism (CBAM) is a praiseworthy initiative: as such, it will simply replicate the European carbon price to imported goods, so that European producers and their international competitors will both pay the same price on carbon, regardless of the place of production. In other words, a perfect plan to reconcile environmental ambition with global trade, in a world where the EU aims to lead the race towards climate neutrality.

CBAM is nevertheless an experiment and with experiments we must be cautious about unintended consequences. As mentioned in the Impact Assessment, CBAM was designed for raw materials and electricity because no solution had been found for downstream products. That means that all manufactured goods (home appliances, electronic devices, etc.) were expected to be out of scope, although they rely on the same raw materials covered by CBAM and would therefore become less competitive than non-EU made manufactured goods.

Take the example of a washing machine made in Europe: the cost of carbon emissions will apply on the aluminium, iron and steel used to produce the device, whether they have been supplied in the EU (subject to the EU-ETS) or imported (subject to CBAM). However, the same washing machine manufactured outside Europe will not be subject neither to the EU-ETS, nor to CBAM. This situation obviously contradicts the objectives of the European Green Deal giving the wrong price signal to consumers, but it will also damage European competition encouraging production delocalisation at the time that. For this same washing machine, EU based manufactures will face at least an increase of 5-10% of manufacturing costs of raw materials to produce one single washing machine. Who do you believe will have to pay for it?

**A complementary legislative proposal to tackle carbon leakage in downstream products**

By putting a price on carbon only for imported raw materials and electricity, CBAM will inevitably encourage carbon leakage down the value chain in all manufacturing sectors using such raw materials. It is a partial solution that will not reach the desired objectives only by itself, quite the opposite.

To make CBAM fit for purpose, it is imperative to prepare a complementary legislative proposal against carbon leakage in downstream products, which will bring the necessary missing provisions to address the case of complex manufactured goods. In essence, downstream products are more complex than raw materials and therefore require a proper methodology. The complementary legislative proposal should at least answer the following questions:

- *Scope and definitions*: how to properly identify downstream products at risk of carbon leakage?
- *Calculation of embedded emissions*: how to measure their relative levels of carbon intensity (and therefore the relative cost on carbon that should apply)?
- *Value-chain traceability*: at which point in the value-chain should CBAM apply?
- *Reporting methods*: how could they be proportionate and coherent, considering the diversity of downstream activities?
- *WTO compatibility*: formally, CBAM only applies to specific categories of goods that are already covered by the EU-ETS, which is not the case for many types of downstream activities. How to ensure consistency with WTO rules?
- *Additional measures*: beyond carbon pricing, which other possible measures should be added to facilitate the relative progression “from brown to green” in third countries?

The European Parliament’s ENVI Committee proposes a scope extension of CBAM to downstream products via delegated acts. We argue that it is a twisted answer that will merely sweep the dust under the rug. It would not suffice to prevent carbon leakage in downstream products, as the current legislative proposal was designed first and foremost for raw materials and electricity. The complexity of downstream products requires a legislative proposal that covers all technical aspects that a delegated act cannot do.

Given the immensity of the task, it is crucial to proceed with clear methodological guidance, temporal predictability and sector prioritisation. The method for carbon leakage risk calculation defined in Art. 10b of the EU-ETS Directive could serve as a compass to detect downstream products at risk of carbon leakage, in a similar way as we have done for years with raw materials. The relative levels of global trade intensity and emissions intensity could reveal downstream sectors mostly exposed to non-EU competition. The complementary legislative proposal would aim at preventing carbon leakage in those sectors, while safeguarding European jobs and competitiveness.