Council of the European Union

Brussels, 15 July 2021
(OR. en)

Interinstitutional File: 2021/0214(COD)

10871/21
ADD 6

ECOFIN 744
ENV 526
CLIMA 191
FISC 122
UD 192
IA 135

COVER NOTE

From:	Secretary-General of the European Commission, signed by Ms Martine DEPREZ, Director
date of receipt:	15 July 2021
To:	Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union
No. Cion doc.:	SWD(2021) 647 final
Subject:	COMMISSION STAFF WORKING DOCUMENT Subsidiarity Grid Accompanying the document Proposal for a regulation of the European Parliament and of the Council establishing a carbon border adjustment mechanism

Delegations will find attached document SWD(2021) 647 final.

Encl.: SWD(2021) 647 final

EUROPEAN
COMMISSION

Brussels, 14.7.2021
SWD(2021) 647 final

COMMISSION STAFF WORKING DOCUMENT

Subsidiarity Grid

Accompanying the document

Proposal for a regulation of the European Parliament and of the Council

establishing a carbon border adjustment mechanism

{COM(2021) 564 final} - {SWD(2021) 643 final} - {SWD(2021) 644 final} -
{SEC(2021) 564 final}

Subsidiarity Grid

1. Can the Union act? What is the legal basis and competence of the Unions' intended action?
1.1 Which article(s) of the Treaty are used to support the legislative proposal or policy initiative?
Articles 191 to 193 of the Treaty on the Functioning of the European Union ('TFEU') confirm and specify EU competencies in the area of climate change. The legal basis for this proposal is Article 192(1) TFEU. In accordance with Articles 191 and 192(1) TFEU, the EU shall contribute to the pursuit, inter alia, of the following objectives: preserving, protecting and improving the quality of the environment, promoting measures at international level to deal with regional or worldwide environmental problems, and in particular combating climate change.
1.2 Is the Union competence represented by this Treaty article exclusive, shared or supporting in nature?
In the case of environment, the Union's competence is shared.
*Subsidiarity does not apply for policy areas where the Union has **exclusive** competence as defined in Article 3 TFEU[1]. It is the specific legal basis which determines whether the proposal falls under the subsidiarity control mechanism. Article 4 TFEU[2] sets out the areas where competence is shared between the Union and the Member States. Article 6 TFEU[3] sets out the areas for which the Unions has competence only to support the actions of the Member States.*
2. Subsidiarity Principle: Why should the EU act?
2.1 Does the proposal fulfil the procedural requirements of Protocol No. 2[4]: - Has there been a wide consultation before proposing the act? - Is there a detailed statement with qualitative and, where possible, quantitative indicators allowing an appraisal of whether the action can best be achieved at Union level?
The Commission engaged in an array of public and targeted consultations, for the preparation of this proposal. An inception impact assessment took place between 4 March and 1 April 2020 with the aim to collect initial feedback on the project. An open public consultation was also placed on the Commission website, from 22 July to 28 October 2020, aiming to gather opinions from citizens and organisations on the justifications, objectives, potential design and scope as well as impacts of the initiative. In addition to these, the Commission services engaged in extensive bilateral consultations with public authorities within the EU and third countries, as well as with business associations, individual companies and NGOs. The impact assessment is explicit in stating that the only meaningful way to ensure equivalence between the carbon pricing policy applied in the EU's internal market -by the EU ETS- and the carbon pricing policy applied on imports is to take action at the level of the Union. CBAM is inherently a border measure and therefore, there is clear added value of placing the intervention at the EU level, although its implementation and enforcement will be better performed at Member States level. These arguments are substantiated qualitatively in the impact assessment.

[1] https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12008E003&from=EN
[2] https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12008E004&from=EN
[3] https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:12008E006:EN:HTML
[4] https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12016E/PRO/02&from=EN

The explanatory memorandum of the proposal and the impact assessment, under chapters 3.2 and 3.3, contain sections on the principle of subsidiarity.

2.2 Does the explanatory memorandum (and any impact assessment) accompanying the Commission's proposal contain an adequate justification regarding the conformity with the principle of subsidiarity?

Climate change is, by its very nature, a trans-boundary challenge that cannot be solved by national or local action alone. Coordinated EU action can effectively supplement and reinforce national and local action and enhances climate action. Coordination of climate action is necessary at EU level and, where possible, at global level, and EU action is justified on grounds of subsidiarity.

Since 1992, the EU has worked to develop joint solutions and to drive forward global action to tackle climate change. More specifically, action at EU level should aim to provide for cost effective delivery of long-term climate objectives, while ensuring fairness and environmental integrity. The establishment of a robust governance of the EU 2050 climate-neutrality objective will help to ensure that the EU remains on track to achieve the objective. Action on climate change adaptation at EU level enables the integration of adaptation policies and measures in key sectors, governance levels and EU policies.

There exists already a harmonised carbon pricing system at EU level: the EU ETS. The EU ETS applies to sectors that are energy-intensive and may be subject to international competition. In order to ensure a well-functioning single market when the EU increases its climate ambition, it is essential that a level playing field is created for the relevant sectors in the internal market. The single effective way to do this is by taking action at the level of the EU. Any initiative needs to be designed in a way that provides importers, regardless of country of origin and port of entry or destination within the EU, with uniform conditions and incentives for carbon emission reductions that are equivalent to those of domestic producers.

Additionally, the need for minimal administrative costs is best achieved by establishing consistent rules for the entire single market, further underlining the added value of an intervention at the EU level. Nevertheless, for the sake of minimising costs and ensuring effective action, national authorities should implement and enforce of the regulation, while a body at EU level could coordinate their actions and provide assistance. This architecture would draw the lessons of the successful experience of the EU ETS.

Moreover, as CBAM is inherently a border measure there is clear added value of placing the intervention at the EU level in view of the fact that external trade is an exclusive competence of the EU. At the same time, the CBAM also needs to be implemented consistently by Member States in the EU market and in view of its close links to the EU ETS, there is further justification of intervention at EU level. The public consultation has confirmed the added value of taking action on the CBAM at the EU level. In particular, stakeholders agree that a CBAM is needed due to existing differences of ambition between the EU and the rest of the world and in order to support the global climate efforts. In addition, in view of the EU's position in international trade, if it introduces a CBAM the environmental effect on international climate ambitions will be most effective as a potential example to follow.

2.3 Based on the answers to the questions below, can the objectives of the proposed action be achieved sufficiently by the Member States acting alone (necessity for EU action)?

This proposal aims to reduce GHG emissions in the EU and avoiding that these emissions reduction efforts are offset by emissions increase outside the EU, as a result of carbon leakage, as well as ensure that the price of imports into the EU reflect more accurately their carbon content. This problem has a cross-border dimension, so it cannot be tackled independently by Member States. Due to its environmental nature and in order to avoid trade diversion, CBAM should be more efficient if designed at EU-level in a uniform way, mirroring EU ETS and designed in a compatible way with WTO rules.

(a) Are there significant/appreciable transnational/cross-border aspects to the problems being tackled? Have these been quantified?

The problem addressed by this proposal is how to succeed in reducing GHG emissions in the EU and avoiding that these emissions reduction efforts are offset by emissions increase outside the EU, as a result of carbon leakage. This risk increases as the EU raises the ambition of its climate policies above that of its trading partners. Therefore, the scale of the problem is commensurate to the raising of the EU climate ambition relative to that of others.

Based on the above, CBAM as a measure –like the problem it addresses - is cross-border one aiming to ensure that the price of imports into the EU reflect more accurately their carbon content. The impact assessment studied in detail the transnational aspects to the problem including impacts on imports and exports of goods subject to CBAM, as well as those indirectly related through upstream or downstream processes. Efficiency and administrative impacts on cross-border flows of goods were also studied in the impact assessment.

(b) Would national action or the absence of the EU level action conflict with core objectives of the Treaty[5] or significantly damage the interests of other Member States?

National action would conflict with core objectives of the Treaty, including the ones in Article 32, which establishes in letter (c) 'the objective of avoiding distorting conditions of competitions within the custom union' and in letter (d) 'the need to avoid serious disturbances in the economies of Member States'. These objectives would be impaired if Member States were left free to adopt individual decisions beyond implementation and enforcement in a matter that involves a number of provisions concerning goods imported in the Customs Union and a number of references to the custom union code.

Moreover, should Carbon Border Adjustment not be applied in a uniform way, it would incentivise behaviours resulting in trade diversion and forum shopping, as third country exporters would import goods through EU jurisdictions applying CBAM in the most lenient way.

Conversely, the absence of EU level action would significantly damage the interests of Member States as established in Article 191 TFEU as the objectives of 'preserving, protecting and improving the quality of the environment' and of avoiding carbon leakage can only be pursued at EU level.

(c) To what extent do Member States have the ability or possibility to enact appropriate measures?

[5] https://europa.eu/european-union/about-eu/eu-in-brief_en

Member States do not have the possibility to enact appropriate measures. If they applied on their own a form of CBAM, they would very seriously risk diverting trade towards Member States not doing so. Moreover, CBAM is designed with a view to mirror the EU emission trading system, an EU wide and harmonised instrument, in terms of price of certificates, phasing out of existing carbon leakage measures and exclusion of third countries.
(d) How does the problem and its causes (e.g. negative externalities, spill-over effects) vary across the national, regional and local levels of the EU?
Member States are exposed to the risk of carbon leakage to different extent. This exposure would depend on whether their economies include industries covered by the EU ETS and more importantly on whether they host particular industrial installations in sectors that are at risk of carbon leakage. Whether a Member State is at EU's external border it may also impact its exposure to carbon leakage. Moreover, differing exposures to the risk of carbon leakage would provide limited justification for action at national level. Carbon emissions are not localised and like the EU ETS, the CBAM can achieve greater efficiency when uniformly applied on a broader scale.
(e) Is the problem widespread across the EU or limited to a few Member States?
Climate change and the need to address it is widespread across the EU.
(f) Are Member States overstretched in achieving the objectives of the planned measure?
No, the measure is proposed to support climate policy in the EU and in Member States.
(g) How do the views/preferred courses of action of national, regional and local authorities differ across the EU?
The European Council invited the Commission to propose a CBAM to ensure the environmental integrity of EU policies and avoid carbon leakage in a WTO-compatible way[6]. As agreed by the European Parliament, the Council and the Commission, the CBAM will also form part of new own resources feeding into the EU's budget[7]. The European Parliament adopted a report on a WTO-compatible EU carbon border adjustment mechanism[8]. National authorities of several Member States also have called for the implementation of CBAM. Regional or local authorities have expressed very few views on CBAM.
2.4 Based on the answer to the questions below, can the objectives of the proposed action be better achieved at Union level by reason of scale or effects of that action (EU added value)?
Reducing GHG emissions is a trans-boundary issue that requires effective action at the largest

[6] European Council. (2020). Conclusions of the European Council of 11 December 2020. (EUCO 22/20 CO EUR 17 CONCL 8).

[7] Interinstitutional Agreement of 16 December 2020 between the European Parliament, the Council of the European Union and the European Commission on budgetary discipline, on cooperation in budgetary matters and on sound financial management, as well as on new own resources, including a roadmap towards the introduction of new own resources (OJ L 433I , 22.12.2020, p. 28).

[8] European Parliament resolution of 10 March 2021 towards a WTO-compatible EU carbon border adjustment mechanism (2020/2043(INI))

possible scale. The EU is well-placed to establish effective climate policy. The introduction of an EU-wide CBAM will create a common and uniform framework to ensure an equivalence between the carbon pricing policy applied in the EU's internal market and the carbon pricing policy applied on imports and it will be beneficial for all.

(a) Are there clear benefits from EU level action?

Yes.

(b) Are there economies of scale? Can the objectives be met more efficiently at EU level (larger benefits per unit cost)? Will the functioning of the internal market be improved?

Yes.

(c) What are the benefits in replacing different national policies and rules with a more homogenous policy approach?

The introduction of a CBAM will not replace national policies, but will create a common framework at EU-level to ensure an equivalence between the carbon pricing policy applied in the EU's internal market and the carbon pricing policy applied on imports.

(d) Do the benefits of EU-level action outweigh the loss of competence of the Member States and the local and regional authorities (beyond the costs and benefits of acting at national, regional and local levels)?

Reducing GHG emissions is fundamentally a trans-boundary issue that requires effective action at the largest possible scale. The EU, as a supranational organisation is well-placed to establish effective climate policy in the EU, like it has done with the EU ETS. An EU-wide CBAM is therefore beneficial for all EU Member States and local and regional authorities. This domestic policy also has transnational aspects, strictly connected with the global dimension of climate change and the objective of curbing global emissions. In particular, the proposed regulation involves several custom aspects that falls in the EU exclusive competence, e.g. custom regimes, import regulations, uniform application of obligations by custom authorities, and agreements with third countries.

(e) Will there be improved legal clarity for those having to implement the legislation?

Yes, since it is a new measure applying to the whole internal market, a single set of rules will ensure uniform application, which will be conferred to Member States authorities.

3. Proportionality: How the EU should act

3.1 Does the explanatory memorandum (and any impact assessment) accompanying the Commission's proposal contain an adequate justification regarding the proportionality of the proposal and a statement allowing appraisal of the compliance of the proposal with the principle of proportionality?

The proposal seeks to address the challenge of reducing GHG emissions in the EU while at the same time avoiding that these emissions reduction efforts are offset by emissions increase outside the EU. The policy choices therefore are clearly dictated by the aim to achieve the objectives of the CBAM, namely to address the risk of carbon leakage in order to fight climate change by reducing GHG emissions in the EU and globally.

The proposed product coverage of CBAM is framed by the sectors and emissions covered by the EU

ETS and the CBAM scope should be laid down by a reference to certain goods by way of their classification in the Combined Nomenclature. This serves the motivation for the measure, namely to ensure that imports of energy intensive products into the EU are on equal footing with EU products in terms of EU ETS carbon pricing and to mitigate risks of carbon leakage. CBAM, as an alternative to free allocation of EU ETS allowances, builds on the logic of the EU ETS starting with sectors where emissions are the highest and therefore where it would matter most.

The carbon content of products is an essential element of the CBAM as it indicates the carbon dioxide equivalent emissions released during their production abroad. This is used to ensure that imported products are treated no less favourably than domestic products produced in EU ETS installations. As installations covered by the EU ETS are subject to a carbon price assessed on their actual emissions, imported products in the scope of CBAM should also be assessed based on their actual GHG emissions. However, such an approach may involve high administrative costs in the beginning and therefore for an initial transitory period it is proposed to use default values with the possibility for the importers to demonstrate that their products were produced with actual emissions lower than the default value, and therefore be subject to a lower CBAM obligation.

As regards the administration of the measure, the choice of empowering national climate CBAM Authorities is meant to minimise administrative costs associated with this task and increase effectiveness. This will require, however, in ensuring proper collaboration and coordination of the assessment of declarations of embedded emissions in imported goods at EU level.

3.2 Based on the answers to the questions below and information available from any impact assessment, the explanatory memorandum or other sources, is the proposed action an appropriate way to achieve the intended objectives?

The legal instrument of a Regulation was chosen to ensure direct applicability, uniform application and uniform enforcement throughout the EU, in order to avoid trade diversion and forum shopping. With a view to ensure a well-functioning measure meeting its climate objectives, a decentralised approach with some coordination and support functions at central level is envisaged in the proposal. Setting up a central CBAM body together with the national climate bodies will minimize the relevant administrative costs associated and will ensure a coherent application of CBAM to all imports. The revenues will finance the implementation costs of CBAM as well as generate new own resources for the EU.

(a) Is the initiative limited to those aspects that Member States cannot achieve satisfactorily on their own, and where the Union can do better?

Yes.

(b) Is the form of Union action (choice of instrument) justified, as simple as possible, and coherent with the satisfactory achievement of, and ensuring compliance with the objectives pursued (e.g. choice between regulation, (framework) directive, recommendation, or alternative regulatory methods such as co-legislation, etc.)?

The objectives of the present proposal can best be pursued through a Regulation. This will ensure direct applicability of a number of provisions concerning goods imported in the Customs Union, included on custom regimes, territorial application, anti-circumvention provisions, or sanctions. Moreover, this Regulation requires uniform and consistent application and enforcement throughout the EU by national authorities in order to pursue the objectives of Articles 32 and 207 TFUE. Any different legal instrument would impair the

needed uniform application throughout the European Union by disrupting competition among Member States and creating unwanted effect of trade diversion and forum shopping. As an example, by choosing the legal instrument of a directive, foreign companies could try to take advantage of different implementation rules of carbon border adjustment in different member states by choosing to import and release products into free practice in Member States applying a more lenient attitude in terms of verification of embedded emissions, sanctions, or guarantees.
(c) Does the Union action leave as much scope for national decision as possible while achieving satisfactorily the objectives set? (e.g. is it possible to limit the European action to minimum standards or use a less stringent policy instrument or approach?)
In order to ensure a well-functioning measure meeting its set climate objectives, a decentralised approach is envisaged. On the one hand, certain tasks where a single approach is key such as the publication of the price of certificates and the establishment default values will be carried out by the Commission, which will also play a role in coordination and advice. On the other hand, national climate authorities will take care of implementation and enforcement tasks, such us the sale of CBAM certificates, the reimbursement requests, the application of penalties. Such system will ensure a coherent application of the CBAM obligations to all imports of the relevant goods in a transparent way, safeguarding the EU's trade obligations and at the same time ensuring an effective application as regards the climate effectiveness of the measure.
(d) Does the initiative create financial or administrative cost for the Union, national governments, regional or local authorities, economic operators or citizens? Are these costs commensurate with the objective to be achieved?
The implementation of CBAM will create limited administrative costs for the Union. The EU will benefit from the increased revenues stemming from the CBAM, which will finance the implementation costs related to the measure and borne by Member States' authorities. It will also generate new own resources for the EU. In terms of impacts to economic operators and citizens, CBAM would entail very limited negative impacts on GDP, investments and consumption in the EU as compared to the case of raising the EU climate ambition in its absence. At the same time, by capturing carbon leakage CBAM would limit output losses in the sectors to which it would apply in view of raising the level of climate ambition. It would also contribute to reduction in emissions in both the EU and in the rest of the world in CBAM sectors by 2030.
(e) While respecting the Union law, have special circumstances applying in individual Member States been taken into account?
Yes as part of the impact assessment the Commission analysis reflected, to the extent possible, the economic and industrial structures of individual Member States as well as their trade flows with third countries. In this context, individual specificities and differences between Member States were accounted for in the assessment of impacts by the Commission.