

CEMA Position Paper on the Carbon Border Adjustment Mechanism

CEMA is the association of the European agricultural machinery industry. CEMA represents both large multinational companies and numerous European SMEs active in the sector. CEMA companies produce a wide range of machines that cover any activity in the field from seeding to harvesting, as well as equipment for livestock management.

By the nature of their businesses, long-term sustainability has always been a priority for CEMA companies. Through precision farming and digitalization EU farmers can now achieve more with less inputs. New Precision Agricultural Technologies increase yields. They also are significantly more friendly to the environment.

CEMA welcomes EU policies and initiatives supporting climate change mitigation through innovation and greater energy efficiency. In this respect CEMA sees the Carbon Border Adjustment Mechanism (**CBAM**), included in the “Fit for 55” package, as a complementary instrument to the international agenda to reduce the CO₂ content of energy-intensive industrial materials and goods, prevent the risk of carbon leakage and support the EU's increased ambition on climate mitigation, while ensuring WTO compatibility.

While CBAM is being drafted by the European Commission, our industry wishes to highlight the principles that it believes are essential to the proper functioning of this future instrument.

1. Impact assessment

CEMA believes that **CBAM must be based on a thorough impact assessment**.

According to the current Commission's proposal, the following goods will be initially covered by CBAM: iron and steel, cement, aluminium electricity and fertilizers¹. For our industry, **steel is a critical raw material**. Depending on the type of equipment, it represents 30-40% of our average production costs. A sudden increase in the price of steel would weaken our industry, and also impact European farmers for whom the price of equipment would increase². For this reason, a rigorous impact assessment of CBAM must be conducted in order to understand the potential effects on the European steel market.

Similarly, fertilizers represent an important part of the production costs of EU farms, and a significant increase in prices could lead to a reduction in their use and decrease in agricultural yields. CEMA companies are working on higher precision methods to apply fertilizers, but farming with broadly reduced levels of fertilizer use would lower yields and thus further increase grain

¹ https://ec.europa.eu/commission/presscorner/detail/en/qanda_21_3661

² An example of the possible effects on the ag machinery industry of steel prices increases can be found at https://cema-agri.org/index.php?option=com_content&view=article&id=820&catid=17&Itemid=213

imports from outside the European Union worsening the ecological footprint of the food-chain in Europe. Further price increase of fertilizers would also place European farmers in a competitively disadvantaged position towards their foreign competitors, who can source fertilizers on their domestic markets and export their production to regions where such a CBAM will not be put in place.

Less competitive EU farmers facing the risk of lower incomes would see a decrease in their capability to purchase new Ag technology, being forced to farm with less efficient, older and less environment-friendly equipment than the newest generations equipped with advanced precision agriculture technologies.

The impact of CBAM on EU global competitiveness should be well-assessed and anticipated. In other terms, we should prevent market fragmentation and measures that would reduce the efficiency of global value-chains.

2. WTO consistency

CEMA stresses the need to have a mechanism consistent with WTO rules so as to keep international trade open and running. Further trade tensions and potential retaliation from trade partners should be carefully assessed for the impact on a balanced sustainable development approach.

The way CBAM will be characterized by the EU will impact the WTO's compatibility assessment. Whether CBAM will qualify as an import tax, a domestic tax or an internal measure affecting trade will make a significant legal difference. In CEMA's view, the CBAM should fall under the domestic regulation category so that the most favoured nation treatment obligation will be respected (Article I:1 GATT 1994).

CEMA also supports key principles and best practices for establishing the future CBAM.

3. Key principles and best practices

For establishing the future CBAM, CEMA subscribes to some of the key-principles and best practices as identified by Aaron Cosbey in his article recently published (27th September, 2021 - <https://www.iisd.org/articles/principles-border-carbon-adjustment-modest-proposal>)

Namely:

a) CBAM should focus on Carbon leakage protection.

It should not create unfair competitive advantages for domestic firms, which would disrupt the well-integrated global agricultural equipment market and production. The CBAM should not be used to coerce other countries to enact predetermined climate policies which would ignore individual country plans to reach the Paris Agreements' goals in their own way.

b) Revenue sharing

In the absence of a rebate for exports, a standalone CBAM limited to EU imports combined with full auctioning would jeopardize the competitiveness of EU producers in export markets even

more. Furthermore, the phase out of free allowances should be accompanied by the introduction of export rebates, in order to address the risk of carbon leakage in export-oriented sectors.

For example, a significant portion of the revenue from the CBAM should be rebated to exporting firms or countries, for example, by lowering producers' costs to comply with CBAM (i.e. fertilizers producers in middle income countries).

c) No additional border-tariff protection

Only the effective carbon price should be levied on imports. Failing to do so involves unfair double protection for domestic producers. Thus, credit for equivalence should be granted for effective carbon prices already borne by foreign goods in the country of export. Such carbon pricing reduces the risk of leakage.

d) Exemption of products covered by anti-dumping, anti-subsidy and safeguard measures

To avoid unnecessary complexity and extra layers of tariffs, detrimental to European producers, CEMA proposes to exempt goods already covered by EU anti-dumping, anti-subsidy and safeguard measures. The list of countries for which CBAM would apply should be adjusted accordingly.

e) CBAM should be part of future or revised EU trade agreements

All future and revised EU trade agreements with third countries should include the Carbon Border Adjustment Mechanism so that trading partners can adjust their policies and reach convergence with the EU. These agreements should foresee meaningful consultation and remediation processes. This includes the possibility to challenge the GHG intensity of foreign goods assumptions. In other terms foreign producers should be able to challenge wrong assumptions by submitting actual data.

f) Call for a Carbon Customs Union

Regarding the existing EU FTA with third countries, CEMA would favour the creation of a Carbon Customs Union by which member countries, committed to the Paris Agreement's goals and having adopted similar level of carbon prices, would impose no Carbon Border Tax to each other. Well designed, this Union could become an attractive organization for other countries which would like to adjust their climate change policies.

g) A Flexible mechanism

As foreseen by the current draft, the CBAM should remain flexible enough to grant equivalences or exemptions to goods covered by other domestic regulations pursuing the same goal. For instance, if the United States would, by 2050, ban fossil fuels it would not be a Carbon Tax, but it will be a domestic measure equivalent to CBAM's objectives.

h) Downstream sectors

CBAM should not be extended to downstream sectors if there is no risk of leakage equivalent to the thresholds used to qualify upstream sectors for coverage.

i) Regulatory simplicity

The European Union is one of the most regulated economies in the world, so care must be taken not to add regulatory complexity. Otherwise, instead of being an engine of new prosperity, the new mechanism would be a new brake on growth and well-being for Europeans. Consequently, CEMA calls for a CBAM with simple and easy-to-use rules for the stakeholders that will have to apply it. In this sense, administrative and financial burdens created by CBAM for businesses that use imported goods in their manufacturing should be kept to a minimum.

ABOUT CEMA

CEMA (www.cema-agri.org) is the association representing the European agricultural machinery industry. With 11 national member associations, the CEMA network represents both large multinational companies and numerous European SMEs active in this sector.

The industry includes about 7,000 manufacturers, producing more than 450 different machine types and generating an aggregated annual turnover of about EUR 40 billion. 150,000 people are directly employed in the sector, with a further 125,000 people working in distribution and maintenance.

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