

POSITION PAPER

Carbon Border Adjustment Mechanism

For a comprehensive green industrial policy and competitive automotive supply chain






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The automotive suppliers' industry supports the Paris Agreement and the even more ambitious objective of climate neutrality. Automotive suppliers are committed to achieve a climate neutral manufacturing footprint and will require access to green steel, aluminium, and other commodity goods to achieve this. CLEPA recognises that climate change justifies timely and tangible action and a policy framework that encourages investments by industry.

-  The policy framework should strike the right balance between introducing cost incentives to trigger private investments and facilitative public investment and other policy measures to alleviate the impact on competitiveness. CLEPA questions whether the current proposal for a Carbon Border Adjustment Mechanism (COM/2021/564) strikes the right balance.
-  Carbon pricing as currently determined through the EU Emissions Trading System (ETS) is one of the key ingredients of the policy framework to realise climate neutrality but poses a significant risk for the competitiveness of EU industry, if other economies do not follow suit. To ensure a level playing field between the EU and countries with potentially lower CO₂ taxation and comparatively less stringent climate protection measures, a form of carbon pricing for imports could be a potential lever. Yet, the current proposal risks to be counterproductive by kicking-off a spiral of protectionist retaliation measures.
-  Therefore, alternatives should be considered first. Furthermore, the current proposal neglects to consider the risks of carbon leakage for downstream industries including the automotive industry and does not provide an answer to the impact that an increasing carbon price may have on the competitiveness of EU exports of processed goods.
-  CLEPA calls on the European Commission, Member States and European Parliament to carefully assess the impact of the CBAM on downstream industries and take a cautious and gradual approach. In its impact assessment the European Commission regrettably did not sufficiently address the potential impact on downstream users of goods subject to the CBAM.



- ✎ Unless a more thorough analysis is conducted, one should consider starting with products that have a predominantly regional and less globalised supply chain, such as cement and electricity. A gradual approach would also allow the Commission more time to engage with international stakeholders, pave the way for international agreements to address the risk of carbon leakage and better reflect the time required to bring down manufacturing related emissions.
- ✎ A comprehensive green industrial policy should aim to reduce the cost difference between climate neutral and carbon emitting production to minimise carbon leakage. Industrial policy will need to be WTO compliant to protect the EU's interests as an export oriented trade bloc.

Policy makers should reconsider the CBAM proposal as an instrument to address carbon leakage risks. CLEPA recommends to:

- 1) Provide more assurance on WTO compliance and pro-active engagement with trade partners to address retaliation and protectionist risks.
- 2) Address carbon leakage risks for downstream industries and avoid a generic import levy that could impose needless costs on EU based automotive suppliers.
- 3) Formulate a comprehensive, WTO compliant, green industrial policy to facilitate a just transformation and reconsider carbon pricing of imports on a unilateral basis as most suitable instrument.

1. CBAM risks for the EU economy and automotive supply industry

1.1 Risks for trade protectionism

In 2020, exports of goods and services accounted for 43.9% of EU GDP (in comparison, for the U.S. this was 11.8% and for China 18.5%¹), highlighting the key role of exports in sustaining the EU's prosperity and a vulnerability to trade conflicts and protectionism. The CBAM is likely to raise significant questions regarding WTO compliance, could trigger retaliation by third countries and may induce other governments to misuse the environmental policy as an excuse to justify protectionist measures, thereby hurting global trade. Already, significant EU trade partners have expressed their concerns about the EU's proposal.

The US envoy on climate, John Kerry, already indicated that the CBAM should be a *"last resort"*² and Brazil, South Africa, India and China released a joint -statement expressing grave concerns *"regarding the proposal for introducing trade barriers such as unilateral carbon border adjustment."*³ Exports resembled 18% of the revenues generated by automotive suppliers in 2020. The aforementioned countries alone

represent 42% of the EU's export of automotive parts, highlighting the sector's vulnerability to retaliation by trade partners and protectionist measures disingenuously framed as environmental policy. CLEPA supports the Commission's commitment to a WTO compliant trade policy and welcomes the emphasis on WTO compliance in the CBAM proposal. Nevertheless, the EU's biggest trade partners are likely to dispute WTO compliance of a potential CBAM proposal and may decide to retaliate before compliance has been legally established.

In case policymakers would go forward with establishing a CBAM, this should therefore be preceded by active engagement with trade partners to avoid a vicious circle of (justified or misplaced) retaliatory tariffs. Exporting producers from third countries that implement environmental policies that achieve a CO₂ output cost comparable to that of the EU should be allowed a workable exemption from the CBAM. Whether countries achieve this through carbon pricing, regulation or standards should not matter. CLEPA shares the Commission's view that the WTO compliance of any CBAM instrument will be linked with a reform of the EU Emission Trading System and a reduction of

¹The World Bank, 21 September 2021: <https://data.worldbank.org/indicator/NE.EXP.GNFS.ZS?locations=EU-US-CN>

²Financial Times, May 2021: <https://www.ft.com/content/3d00d3c8-202d-4765-b0ae-e2b212bbca98>

³Euractiv, 12 April 2021: <https://www.euractiv.com/section/energy-environment/news/emerging-economies-share-grave-concern-over-eu-plans-for-a-carbon-border-levy/>



available free allowances, but the pace with which this is implemented needs to be carefully assessed.

More importantly, all revenues generated by the CBAM should be reinvested through a fund for industrial climate innovation of which all CBAM affected industries could benefit. This fund could be one of the means through which the risk of carbon leakage in its broadest sense could be addressed. The current proposal to let revenues flow into the general EU budget⁴ therefore lacks ambition and may even undermine a potential legal WTO case.

1.2 Risks for downstream industrial sectors

The automotive industry is globally integrated with a strong localised manufacturing presence close to the customer where appropriate. Automotive suppliers source most of their steel and aluminium from European mills and the automotive industry as a whole is responsible for 16% of the demand for European steel⁵ and 36% of European aluminium⁶. Nevertheless, certain materials used in the automotive industry cannot always be provided in the quantities or qualities required by European industries.

The current CBAM proposal introduces a generic levy on a four-digit HS code level for steel and aluminium products. The proposal ignores the fact that the EU producers of steel and aluminium do not have sufficient capacity to supply automotive suppliers with the full range of processed steel and aluminium involved in the production of the up to 30,000 parts and components needed to build a car.

Steel and aluminium for which no sufficient EU capacity exists, includes certain steel bars for crankshaft, pignons, gearshaft, connecting rods, components for ground rail and bearings and flat-rolled aluminium products used to produce body parts or automotive heat exchangers critical for the thermal management of both internal combustion engines and (an even more critical for) electric vehicles. A carbon border adjustment mechanism that generically imposes a levy on imports of steel and aluminium products at a four-digit HS level would fail to sufficiently reflect the reality of specialised global supply chains. As a result, CBAM may increase the costs of these resources without protecting European resource industries and instead hamper the competitiveness of industries relying on imports for certain raw materials. The increasing

⁴Page 10 of the 'Proposal for a Regulation establishing a carbon border adjustment mechanism' states that most revenues generated by the CBAM will go to the EU budget.

⁵[EUROFER, European Steel in Figures 2021, 17 June 2021](#)

⁶[European aluminium, Support for the recovery of the automotive sector, 18 May 2020](#)

prevalence of anti-dumping and safeguard duties only reinforce the cost pressure for suppliers who have no domestic sourcing alternative for some of their imports. Part of the objective of a more extensive impact assessment on downstream industries could be to determine a list of HS codes and sectors for which (temporary) exemptions should be considered.

1.3 Risks for a level playing field

EU suppliers of automotive parts face increasing competition from suppliers established outside of the EU in countries like Morocco, Serbia and Ukraine. CLEPA is concerned that the introduction of a CBAM on steel and aluminium will distort the level playing field of, for instance, foundries relying on imports for part of their sourcing to produce processed parts of steel and aluminium.

The CBAM rightly does not impact the import of automotive components in this stage. Tracking CO₂ emissions throughout the long and globally integrated automotive supply chain is still too complex and carbon leakage risks will highly depend on the type of component and the relation

between logistical and production costs. The CBAM levy on steel and aluminium in its proposed form, however, risks distorting the level playing field. While a producer of engine, transmission or body parts located in the EU will face higher material costs due to the CBAM levy on his imports, his competitor located outside of the EU is not affected by the CBAM and may maintain access to the single market without being affected by any form of carbon pricing.

1.4 Risks for industrial transformation

The automotive industry is facing the biggest transformation in its history, researching, developing and bringing to market the solutions that will allow carbon neutral transport. In 2020, the 11 biggest European-headquartered suppliers alone invested €19.4 billion in research and development⁷.

Material costs will play a huge role in determining the margins and therefore room for investment of automotive suppliers. An increase of material costs could render EU member states less competitive and therefore accelerate job losses linked to the phasing out of the combustion engine for large parts of personal transport.



The driving train of an internal combustion engine vehicle alone has more than 2,000 moveable parts versus 20 moveable parts for an electric vehicle.

Furthermore, the production of electric power-trains requires up to 70% less labour than a combustion engine⁸, and automotive suppliers will have to restructure their supply chains as electric vehicles will increasingly dominate private personal traffic. Lower volumes in the internal combustion area business will result in relatively higher material costs as scale advantages disappear.

These effects will be exacerbated by an increasing carbon price and the introduction of a CBAM levy and create a risk that internal combustion engine related employment will be consolidated outside of the European Union in countries that do not have a CBAM or equivalent form of domestic carbon pricing in place. A quicker loss of internal combustion engine related employment (30-40% of the sector's overall employment) will increase the pressure on regional economies and reduce the time available to reskill workers for jobs related to the carbon neutral economy.

⁸Fraunhofer IAO, Beschaeftigung 2030, December 2020



Policy recommendations for an effective CBAM proposal



- 1. Provide more assurance on WTO compliance** and pro-active engagement with trade partners to address retaliation and protectionist risks



- 2. Address carbon leakage risks for downstream industries** and avoid a generic levy that could impose needless costs on EU based automotive suppliers



- 3. Embed any form of carbon pricing for imports in a comprehensive green industrial policy** and avoid a levy that exacerbates the social dimension challenge of the industrial transformation

2. Need for a comprehensive green industrial policy

Automotive suppliers have a strong interest in levelling the playing field between CO₂-emitting and CO₂-neutral produced commodities, as we are committed to the Paris agreement and a climate neutral manufacturing and supply chain footprint.

For an internal combustion engine vehicle, 21 to 27% of the CO₂ lifecycle emissions are related to material production. McKinsey estimates that as electric vehicles become more dominant, the share of material production in life-cycle emissions is likely to increase to 35% in 2030 and 60% in 2040⁹. A significant enough fund that supports the development of CO₂ neutral production technologies could help automotive suppliers access green material inputs, including steel, aluminium and battery chemicals and offset at least part of the impact of the ETS and CBAM on Europe's competitiveness. Public-private cooperation and investment together could help Europe establish a green industrial base that remains competitive without a structural carbon levy on imports.

Unfortunately, the current CBAM proposal foresees that proceeds of the CBAM will flow into the EU budget and the repayment of

'NextGenerationEU'. The national recovery plans linked to 'NextGenerationEU' lack ambition and direction on support for the green transformation of industry. Automotive suppliers are concerned that the current proposal will impose an unbalanced levy on industry, distort competition along the value chain, provide insufficient support to industry to address competitive challenges and believe the Commission underestimates the impact that trade conflicts may have on export revenues and the resilience of Europe's industrial base.

A more gradual introduction and more extensive impact assessment of the introduction of CBAM on downstream users of steel and aluminium would therefore be an absolute prerequisite to ensure that the CBAM can play a positive role in establishing a competitive, climate neutral European industry.

[Would like to know more?](#)

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⁹[McKinsey & Company, The zero carbon car, 18 September 2020](#)

CLEPA, the European Association of Automotive Suppliers, represents over 3,000 companies supplying state-of-the-art components and innovative technologies for safe, smart, and sustainable mobility.

CLEPA brings together over 120 global suppliers of car parts, systems, and modules and more than 20 national trade associations and European sector associations. CLEPA is the voice of the EU automotive supplier industry linking the sector to policy makers.

- The automotive sector accounts for **30% of R&D** in the EU, making it the number one investor.
- European automotive suppliers invest over **30 billion euros** yearly in research and development.
- Automotive suppliers register over **9,000 new patents** each year.
- Automotive suppliers in Europe generate **1.7 million** direct jobs.

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