The EU CBAM's reform and remaining implementation challenges for low- and middle- income countries

Since its inception, the EU's **Carbon Border Adjustment Mechanism (CBAM)** has sparked international concern, particularly among **low- and middle-income countries (LMICs),** over fairness, feasibility, and economic impacts. Tensions around the mechanism's full-scale implementation, delayed to 2026, culminated on 19 May 2025 with a first formal complaint against the measure **filed by Russia before the World Trade Organisation's Dispute Settlement System**, which the EU considers "unfounded". This destabilisation attempt from Russia further highlights the diplomatic dimension of a measure that has become a **global symbol of the EU's externalisation of climate efforts**. Following the adoption by the European Parliament (22 May) and the Council (27 May) of a series of amendments to simplify the CBAM regulation, this brief summarises recent domestic CBAM developments, analyses implications for developing countries, and offers pathways for greater global carbon market interoperability and equity.

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Adopted in 2023, the Carbon Border Adjustment Mechanism (CBAM) aims to protect the integrity of the EU's Emissions Trading System (ETS) by preventing carbon leakage and ensuring that imported goods face equivalent carbon pricing. Since its inception, the mechanism has sparked international concern over

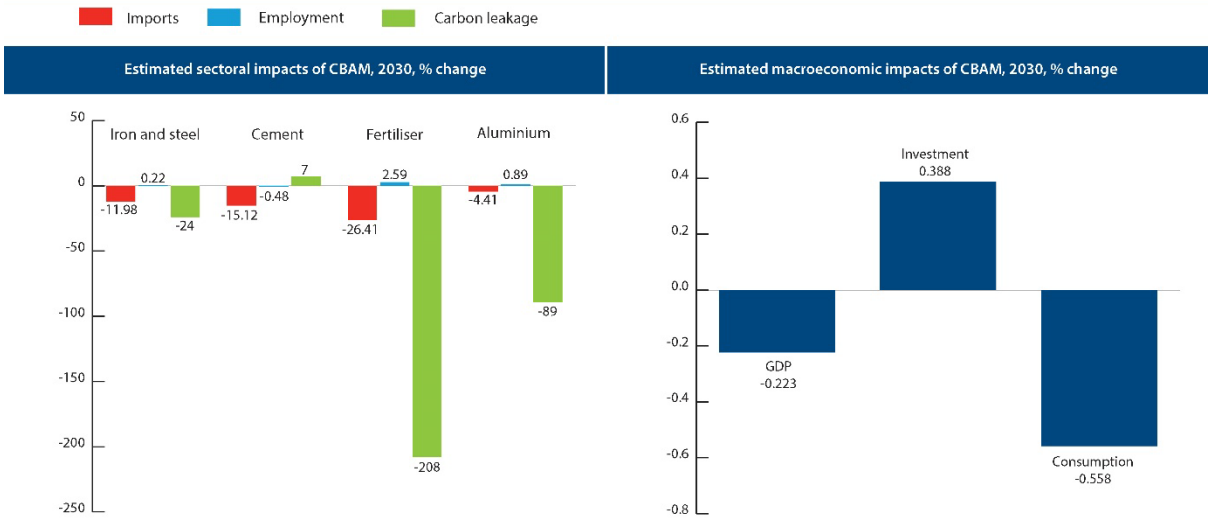
fairness, feasibility, and economic impacts, particularly among low- and middle-income countries (LMICs). Tensions around the mechanism's full-scale implementation, delayed to 2026, culminated on 19 May 2025 with a first formal complaint against the measure filed by Russia before the World Trade Organisation's Dispute Settlement System. As climate urgency increases and the EU faces the need to triple its emission reduction pace to meet its 2030 targets compared with the last decade (European Commission 2024), CBAM has become a global symbol of the EU's externalisation of climate efforts. A few days after the adoption by the European Parliament of a series of amendments to simplify the regulation, this brief summarises recent domestic CBAM developments, analyses implications for developing countries, and offers pathways for greater global carbon market interoperability and equity.

1. CBAM implementation: domestic progress and challenges

a) Transition phase dynamics

Since October 2023, importers must report embedded emissions but are not yet required to purchase CBAM certificates. This transitional phase has had limited observable impact on trade flows, though full implementation (planned for 2026 or later) is expected to affect production and sourcing patterns significantly. While CBAM's macroeconomic impact on the EU is minor (−0.22% GDP by 2030), sectoral effects are notable: EU imports of fertilisers may fall by 26%, with iron and steel also heavily affected. Variability across member states (e.g. Bulgaria, Ireland, Greece) highlights regional sensitivities tied to import dependencies.

Figure 1: Estimated macroeconomic impact of CBAM in the EU



Source: European Commission, 2021

b) Administrative and technical hurdles

A key challenge for importers is calculating embedded emissions using installation-specific data, a requirement enforced since July 2024. While default data are still permissible in limited cases, most declarants must now rely on complex supply chain reporting—often hindered by data unavailability from third-country suppliers. This has placed disproportionate burdens on small and medium-sized enterprises (SMEs), both within and outside the EU. To address these concerns, the Commission proposed in February 2025 to:

- Raise the de minimis threshold to 50 tons/year, supposedly exempting ~90% of importers by volume.

- Allow use of default values without justification.

- Reconsider full CBAM rollout, possibly delaying it to 2027.

The political atmosphere in the European Parliament regarding the EU CBAM has shifted significantly since the previous legislative term, to the extent that the mechanism now stands out as one of the most broadly supported pieces of the EU's climate policy puzzle. Over 2,000 amendments were originally tabled in response to the initial CBAM proposal. By contrast, in the current legislative cycle, specifically within the framework of the Omnibus I regulation, only around thirty amendments have been submitted on CBAM. On 22 May 2025, the European Parliament endorsed the proposal of the European Commission to introduce a de minimis threshold of 50 tonnes under the EU Carbon Border Adjustment Mechanism (CBAM), a move aimed at simplifying compliance for SMEs and occasional importers. According to the European Commission[1], this new threshold would exempt 90% of importers—primarily small businesses and individuals—while still covering 99% of CO_2 emissions from imports of iron, steel, aluminium, cement, and fertilisers. This replaces the previous €150-per-shipment exemption, which proved ineffective, disproportionately burdensome for small businesses, and easily circumvented through shipment splitting. Changes in the amendments adopted by the European Parliament on 22 May – and which will now have to be negotiated between the Parliament and the EU Council streamline the authorisation process for declarants, simplify emissions calculations and liability management, and reinforce anti-abuse measures. The

[1] **COM(2025) 87 final, 2025/0039 (COD)** Proposal for a Regulation of the European Parliament and the Council amending Regulation (EU) 2023/956 as regards simplifying and strengthening the carbon border adjustment mechanism, Brussels, 26.2.2025
See new methodology under Annexe II, revising Annexe VII of the Proposal to dynamically continue to cover 99% of emissions https://commission.europa.eu/document/download/dc72f9cb-2b58-465a-8a33-8c5d6b6efe8b_en?filename=COM_2025_87_annexes_EN.pdf

reform proposes allowing importers to choose between using actual emissions data or conservative default values, making compliance more accessible for countries with limited monitoring capacity and encouraging the use of verified data. Finally, under the proposed reform and in response to challenges in documenting foreign carbon pricing at the product level, the Commission will develop default carbon price values by country or regime, ensuring that foreign carbon prices can be deducted from CBAM obligations more systematically. Additional adjustments include delaying the start of CBAM certificate sales to February 2027 (for 2026 emissions), extending reporting deadlines, and excluding downstream emissions in steel and aluminium, which are deemed to have limited climate relevance.

c) Gaps in circularity and scope

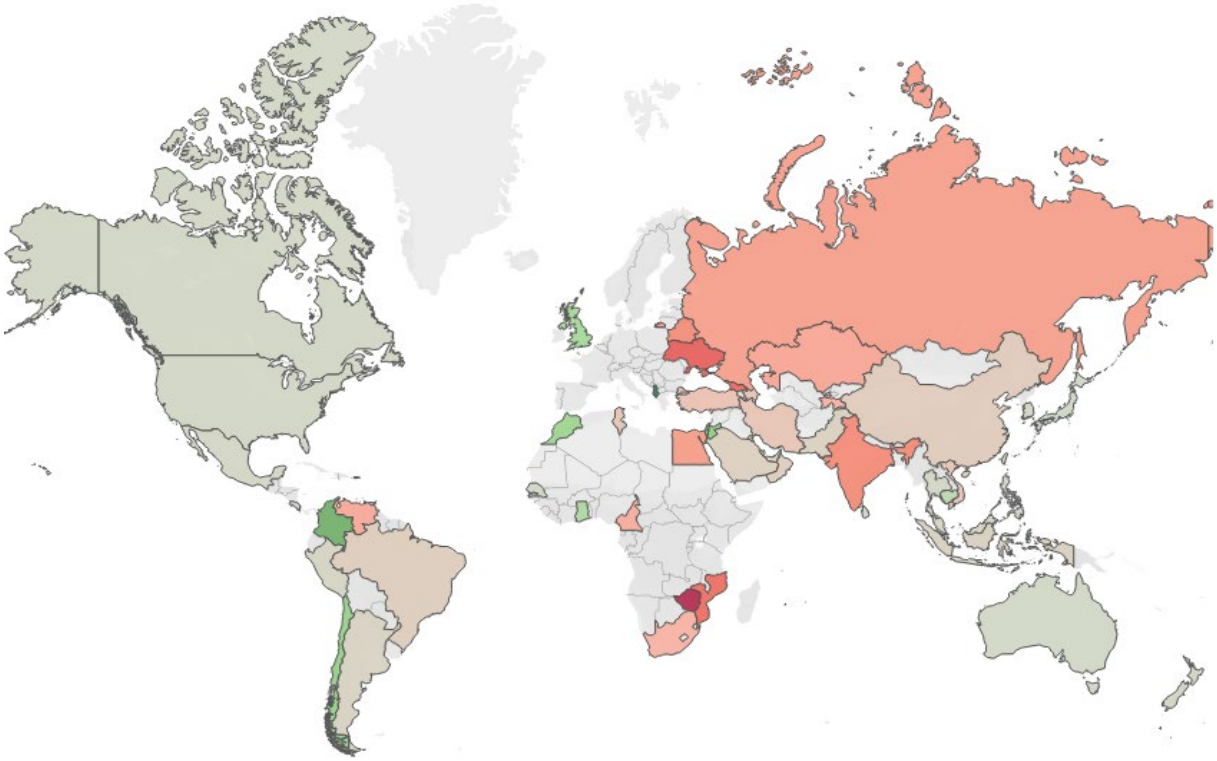
CBAM's current design excludes downstream products and scrap materials, reducing incentives for circular value chains and undermining EU objectives for a resource-efficient single market. Business groups have called for extending CBAM to downstream products like aluminium and steel to support recycling investments and prevent regulatory arbitrage. A growing concern is the so-called "scrap loophole" (Sandbag, 2024) which allows exporters to circumvent the CBAM by blending high shares of recycled pre- or post-consumer scrap into products destined for the EU— thereby lowering reported emissions without actually reducing average carbon intensity. This legal circumvention undermines the level playing field CBAM seeks to create, especially as EU producers face more limited access to high-quality scrap and are phasing out free allowances. Moreover, the current reliance on actual emissions data encourages resource shuffling and under-reporting, since importers can selectively declare low-carbon goods with real data while defaulting to less accurate reporting for higher-emission products. A systematic use of country-level default values could close this loophole, reduce complexity and compliance costs, and align incentives more effectively toward actual emissions reductions across entire supply chains.

2. CBAM's impacts on Global South countries

a) Trade exposure and structural vulnerability

Countries face CBAM exposure through two channels: high absolute exports to the EU (e.g. China, India, Türkiye), or strong economic reliance on CBAM sectors (e.g. Zimbabwe, Ukraine, Georgia). LMICs in the second group are particularly vulnerable, as even low export volumes can significantly affect local economies. The World Bank's CBAM Exposure Index flags several LMICs at high aggregate risk, particularly in fertilisers and cement. Africa, despite limited exports, faces high ad valorem rates and stands to lose up to 0.5% of income due to potential trade declines (African Climate Foundation and The London School of Economics, 2023).

Figure 2: Aggregate relative CBAM exposure index



Source: World Bank (2025)

b) SME disadvantage and value chain fragmentation

SMEs in LMICs are indirectly affected through their role in complex supply chains. As EU importers push compliance costs downstream, SMEs lacking data management or decarbonization capacity face financial strain and potential exclusion from value chains. Multinational firms with dual EU/non-EU operations (e.g. Tata Steel) may adapt more easily, but this bifurcation risks widening structural inequalities. The main concern is not just direct costs, but cascading impacts through indirect enforcement, client renegotiations, and administrative compliance.

3. A global patchwork: carbon pricing and interoperability

a) Growing but fragmented landscape

As of early 2025, 58 emissions trading systems exist globally—up from 29 in 2019. While momentum is growing, significant disparities persist in coverage, price levels, and scope. The EU ETS price remains the highest globally (US$70–80/ton), while systems in China, South Korea, and California vary widely in ambition and administrative burden. Despite shared sectoral targets (e.g. industry, power), deeper interoperability remains elusive. The complexity and fragmentation raise costs for global firms and risk inefficient decarbonization.

b) Towards greater convergence

Several countries (UK, Türkiye, China) are considering or have introduced CBAM-like mechanisms. The UK plans a system by 2027, offering potential for EU alignment (Lydgate and Winters, 2025), as the EU and the UK officially announced working on the integration of their respective emissions trading systems, which would imply a mutual recognition of their Border Adjustment Mechanisms. The EU has joined Canada's Global Carbon Pricing Challenge, aiming to harmonise approaches, but the initiative lacks LMIC participation. The EU's proposed default recognition of foreign carbon prices is a step forward, but broader recognition of alternative mitigation efforts, such as green investment projects or internationally accepted carbon accounting standards, may be needed. Brazil, for instance, has advocated for the inclusion of ISO and GHG Protocol standards (International Institute for Sustainable Development, 2024)

c) Financing a fair transition

CBAM is expected to generate €2.1 billion annually in EU revenues. While the regulation prioritises domestic reinvestment, several stakeholders have called for a share of these revenues to be earmarked for international climate finance, especially to support industrial decarbonization in LMICs. A promising recent proposal (Sandler, 2024) involves recognising green investments in exporting countries as part of their domestic carbon pricing equivalent, effectively channelling CBAM revenues into decarbonization projects abroad. This would ensure both climate and development dividends, while fostering political buy-in.

Conclusion and recommendations

While essential to the EU's net-zero trajectory and the integrity of the EU ETS, its success hinges on broader legitimacy and international cooperation. To mitigate tensions and avoid widening global inequality, the EU should:

1. Finalise simplification reforms to ensure SMEs, both in the EU and globally, are treated equitably
2. Expand CBAM scope to incentivize circular economy practices and capture emissions from downstream products.
3. Support LMIC readiness through financial and technical assistance for MRV systems and carbon pricing instruments.
4. Enhance international alignment by recognizing alternative mitigation efforts and participating in carbon pricing dialogues.
5. Allocate part of CBAM revenues to global climate finance, linking them to measurable decarbonization outcomes in exporting countries.

The future of CBAM depends not only on its robustness but on its ability to catalyse global climate cooperation without leaving the Global South behind. Debunking its divisive potential will be key to the EU's strategy to deliver ambitious outcomes at COP30. If so far only Russia has challenged the measure before the WTO, a way to ease tensions could be – in the context of the G20 – to reach a ministerial declaration of non-challenge at the WTO assorted with an agreement to work on interoperable regulatory solutions on carbon mitigation approaches.

Key Recommendations

1. Finalise simplification reforms to ensure SMEs, both in the EU and globally, are treated equitably
2. Expand CBAM scope to incentivize circular economy practices and capture emissions from downstream products.
3. Support LMIC readiness through financial and technical assistance for MRV systems and carbon pricing instruments.

4. Enhance international alignment by recognizing alternative mitigation efforts and participating in carbon pricing dialogues.

5. Allocate part of CBAM revenues to global climate finance, linking them to measurable decarbonization outcomes in exporting countries.

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