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Preparing for the Carbon Border Adjustment Mechanism ("CBAM")

The CBAM in the Life Sciences and Healthcare (LSHC) industry

While the LSHC industry may not be the first industry that comes to mind when assessing the impact of the CBAM, its relevance should not be underestimated. For instance, as the most common metal used in the manufacturing of medical equipment, stainless steel is key to the health care sector, while aluminum foil is used in the blister packaging for medicines. On the other hand, Maintenance, Repair, and Operations (MRO) activities will be affected across the industry, touching both the medical devices and the pharmaceutical sectors.

What is CBAM?

As part of its "Fit for 55 Package," the European Union (EU) launched a comprehensive set of legislative proposals and initiatives. The goal of this program is to align the EU's climate and energy policies with its ambitious target of reducing net greenhouse gas emissions by at least 55% by 2030.

The *Fit for 55 Package* includes the introduction of the CBAM, which is an environmental policy tool designed to make sure that imported products bear the same carbon costs as those incurred by operations within the EU. By doing so, the CBAM addresses the risk of the EU's climate goals being compromised by "carbon leakage," the shift of production to countries with less stringent decarbonization policies.

During its definitive phase, importers of specific goods, represented by EU authorized declarants, will buy and use CBAM certificates corresponding to the embedded emissions of their imported products.

These certificates' prices will be influenced by the EU Emission Trading System (EU ETS) allowance price, and the Monitoring, Reporting, and Verification (MRV) rules will align with the EU ETS's MRV system, achieving parity in carbon pricing between imported and domestically produced goods.

The CBAM transition phase (2023-2025)

Regulation (EU) 2023/956[i] outlines the reporting requirements for the CBAM during the transition period, from 1 October 2023 to 31 December 2025.

Throughout this period, EU importers (or their indirect customs representatives, where relevant) have to provide reports on imported goods, encompassing quantity, direct and indirect emissions contained within, and associated carbon costs for these emissions, including those from precursor materials (i.e., relevant products components). The first report, covering imports from October to December 2023, had to be submitted by 31 January 2024 and subsequent reports will be due quarterly.

This transition phase aims to gather data to refine the methodology for calculating (in)direct embedded emissions for the implementation phase. This collected data and insights will also inform the EU Commission for the establishment of a monitoring, reporting, and verification methodology post-transition.

If dealing with CBAM goods imported into the EU, importers will contact foreign installations for "embedded emissions" data. Preparing to provide this information promptly is essential.

The CBAM will take full effect on 1 January 2026, with importers obligated to purchase CBAM certificates for each imported CBAM good at the average EU ETS allowance price. This obligation's scope will gradually increase after 2026, covering complete embedded emissions by 2034.

The CBAM will apply to all goods exported to the EU falling under Annex 1 of the CBAM Regulation, i.e., certain goods and selected precursors with carbon intensive production, which present the most significant risk of carbon leakage: cement, iron and steel, aluminum, fertilizers, electricity, and hydrogen.

Is CBAM relevant for your operations?

Stainless steel

Stainless steel's unique combination of mechanical, chemical, and hygiene properties makes it an indispensable material in medical equipment due to its corrosion resistance, durability, and ease of sterilization. Stainless steel is found in many surgical instruments such as scalpels, but also implants and prosthetics, medical carts and trays, dental instruments, autoclaves, or even hospital furniture in general.

The steel products that are within the scope of he CBAM are varied, encompassing most of Chapters 72 and 73 of the Harmonized System (HS) and including, among others, 7218 “semi-finished products of stainless steel”, 7304 “tubes and pipes”, 7310 “drums, cans, boxes and similar containers”, 7318 “screws and bolts”, and more broadly 7326 “other articles of iron and steel”.

Aluminum

The aluminum sector has a complex downstream value chain, and its (semi)-finished products have many uses. One of them, “aluminum foil,” classified under heading 7607, is a key component of the blister packaging for tablets and, more generally, for most of the medicines put up in measured doses. The aluminum is indeed known for its reliable protective properties which makes it the ideal candidate for sensitive pharmaceutical products as it provides protection from moisture and oxygen, extending the product’s shelf life.

Aluminum being part of the CBAM scope alone could drive some of the actors in the pharmaceutical industry to consider some relocation of their aluminum foil sourcing streams within the EU to limit the reporting burden resulting from the CBAM.

MRO

While often overlooked, MRO products do constitute a crucial and strategic part of manufacturing activities and include the type of goods that are not always linked to the finished product category. The vast array of MRO goods includes, among other things, maintenance and repair tools, production machinery equipment, and spare parts.

Similarly, many MRO related products will be categorized in Chapter 73, which is in scope of the CBAM regulation.

Reporting requirements

During the transition period (1 October 2023 to 31 December 2025), EU importers of products subject to CBAM will need to report a given set of information on a quarterly basis.

The reporting declarant (i.e., the EU importer or its representative) must submit these CBAM reports to the CBAM transitional registry (electronic repository) no later than one month after the end of each quarter. A reporting declarant may modify a submitted CBAM report up to two months after the end of the relevant reporting quarter.

The report should include, but is not limited to, the quantity of the CBAM goods imported into the EU, their HS codes and country of origin, details on the installation (facility) where the goods were produced, their production routes, and their embedded carbon emissions expressed in CO_2e per ton.

The greenhouse gas (GHG) emissions to be reported include direct (resulting from the production of the goods) and indirect (resulting from the electricity consumed during the production) emissions as well as the emissions of the precursors, i.e., relevant raw materials used to produce the goods.

Financial Impact

Based on the default value determined by the EU Commission for the steel sector, the categories of goods mentioned above have, on average, more than two tons of CO_2e per ton of steel products. Aluminum foil, on the other hand, is skyrocketing to above 12 tons of CO_2e per ton of aluminum produced (of which nine tons result solely from indirect emissions).

Although recent predictions in the beginning of 2024 forecasted lowered prices for EU carbon permits due to the general economic outlook, which translated into weak demands on the EU ETS market, the average forecast has been set at €74.11 per metric ton for 2024 and €83.31 per metric ton for 2025. However, the average forecast for 2026—the year of the entry into force of the CBAM certificates and the beginning of the financial impact on EU importers of CBAM relevant goods—still reaches €100.13 per metric ton[ii].

In this context, EU importers of CBAM products relevant to the health care industry can take into account an extra cost of €150 to €200 for each ton of imported steel products, and at least €1,000 for aluminum products.

Recommended next steps

The first step should be to undertake an analysis to identify whether products in your overall chain of supply and imported into the EU market are relevant for the CBAM. Take a broader lens to include MRO activities and products, research and development activities, as well as clinical trials, rather than focusing only on your core commercial products.

In this first analysis, your organization's data availability and quality will be of strategic importance. Most importantly, your products' HS classification codes must be duly determined and assigned as it will drive the next steps and requirements.

Once relevant products have been identified, the subsequent requirements will depend on your position in the supply chain and will mostly differ whether you are an importer or a supplier of CBAM relevant goods.

For EU importers

If you are an EU importer, you must report and, as of 2026, pay for the carbon emissions embedded in relevant products you import into the EU. First, you should identify who your suppliers are and contact them to understand whether they have started to collect the necessary data you will need to report to the authorities.

While the EU has offered some flexibility and the possibility to rely (partially) on default data during the first year of the CBAM implementation, it is crucial to confirm that your suppliers will have the data you will need at their disposal.

Second, you should perform a supply chain review and analysis of the most carbon emissions efficient suppliers to manage the additional financial burden that will become a reality beginning in 2026.

For manufacturers and/or suppliers of CBAM products to the EU market

If you manufacture or supply products, you must gather the data required regarding the carbon emissions embedded into the products you are exporting to the EU. This includes emissions of certain materials (precursors) used in the production of end-products, so you also need to liaise with your suppliers and customers down and up the value chain for a complete and accurate picture of your emissions production routes.

It is also highly recommended that you perform a GHG assessment and identify ways to reduce your GHG emissions given that the financial burden will be imposed directly on your end customers, which no doubt will have an impact on your competitiveness during commercial negotiations.

Along with the EU CBAM, also consider new reporting obligations and carbon market schemes that are being implemented (or at the very least being considered) in many other jurisdictions such as, among others, the UK (2027), Japan (2028/2029), Australia (TBD) and the US (TBD).

Finally, other ESG-related legislation is being implemented in the EU, which will also have an impact on the supply chains of all European businesses and will not spare the LSHC industry. These include the EU Deforestation Regulation as well as the Corporate Sustainability Reporting Directive.

For more information on the impact of those regulations on your operations, please don't hesitate to contact us:

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[i] Regulation (EU) 2023/956 of the European Parliament and of the Council of 10 May 2023 establishing a carbon border adjustment mechanism https://eur-lex.europa.eu/eli/reg/2023/956/oj

[ii] The average forecast for EU Carbon pricing for 2026 reaches €100.13 a ton. https://www.reuters.com/markets/commodities/analysts-forecast-eu-carbon-price-rise-say-supply-could-swell-2024-07-23/
Source: Reuters