itm Irish Tax Monitor

The Roundtable August 2023

Carbon Tax

The EU's Carbon Border Adjustment Mechanism (CBAM) will apply from 1st October 2023. What are the implications for taxpayers and how can corporates prepare for the new rules?

Dr. David Savage, Senior Manager, Customs and International Trade Services, BDO: CBAM is one of the initiatives included the EU's 'Fit for 55' suite of measures that seeks to deal with the issue of carbon leakage. Carbon leakage occurs when, due to the expense of complying with the EU's stringent climate policies, manufacturers may seek to move their carbon intensive operations to jurisdictions with more lax climate regulations thus undermining the EU's anti-climate change measures. CBAM will affect imports of iron/steel, aluminium, cement, fertiliser, electricity and hydrogen and will complement the EU's main emission reduction scheme, i.e., the Emissions Trading Scheme (ETS).

Currently, an ETS operates for certain domestic installations within the EU. As part of this scheme, the level of greenhouse gas (GHG) emissions within the EU are capped on an annual basis. This cap on emissions is being gradually reduced year-on-year. As the availability of ETS allowances decreases over time, the cost of emitting GHGs in the EU goes up. Therefore, without CBAM, an incentive exists to move manufacturing outside of the EU. CBAM will mirror ETS by placing a charge on carbon-intensive goods when they are imported into the EU.

Dr. David Savage

When fully implemented in 2026, importers will have to purchase CBAM certificates to cover the GHG emissions embedded in affected products being imported into the EU. CBAM therefore, will effectively equalise the cost of carbon emissions embedded in imported goods relative to those goods subject to the ETS and which are manufactured within the EU.

In October 2023, the CBAM transitional period begins. During this time, there will be no charges levied on imports of affected goods but importers will have to report emissions data on a quarterly basis. The CBAM report shall be submitted via the CBAM Transitional Registry which will be available for use from the 1st of October 2023.

Though no CBAM charges will be imposed until January 2026, the introduction of CBAM will bring a new administrational burden on companies, many of whom are already struggling with staff shortages. Irish businesses that import CBAM goods from outside of the EU/EEA will be required to gather emissions data from their non-EU/EEA supplier and submit quarterly reports. With the first CBAM report due in January 2024, now is the time to understand what compliance with CBAM measures will mean for your company.

Irish businesses should now begin reviewing their supply chains. It is recommended to review the Combined Nomenclature (CN) codes of imported goods and ensure that the assigned codes are accurate. Then determine if these CN codes are listed in Annex I of Regulation (EU) 2023/956. If it emerges that your company has an exposure to CBAM, it will be necessary to ask your non-EU supplier to provide emissions data.

ESG and the Tax Function

Companies have and are making business decisions to align policies and procedures with new ESG and sustainability strategies. Can you discuss the role the tax function can play to ensure such strategies and decisions can avoid negative tax consequences for the company?

Carol Lynch, Partner, Customs and International Trade Services, BDO: Businesses today are increasingly adopting and articulating tax principles, aligned to their broader Environmental, Social, and Governance (ESG) agenda.

In the modern world external stakeholders are increasingly interested in a business's corporate and income tax behaviors and expect to see evidence of the level of tax responsibility it adopts in terms of aggressive tax strategies as well as the level of economic contribution the business makes to society.

This is also vital in the M&A space where an investor's ESG program will include evaluation of the investee entity's tax framework.

In response, many businesses are publishing wider tax statements and also signing up to increasing transparency standards including the OECD/G20 Principles of Corporate Governance, the GRI (Global Reporting Initiative) for comprehensive tax disclosure and the International Business Council (IBC) of the World Economic Forum – Stakeholder Capitalism Metrics.

In Europe, the CSRD Directive will

Carol Lynch

also come into effect for FY 2024. The first companies will have to apply the new rules for the first time in the 2024 financial year, for reports published in 2025.

Companies subject to the CSRD will have to report according to European Sustainability Reporting Standards (ESRS). The standards were developed by the EFRAG, an independent body bringing together various different stakeholders. The standards are tailored to EU policies, while building on and contributing to international standardisation initiatives.

The CSRD requires assurance on the sustainability information that companies report and will provide for the digital taxonomy of sustainability information.

When we look at the areas of tax which most specifically fall within the ESG agenda we see these as:

1) Tax and the Environment: for example, carbon taxes, plastic taxes; CBAM, green subsidies and investments, deforestation regulations
2) Social taxes such as PRSI, USC, flexible workforce, gig economy, supply chain ethics and transparency
3) Governance and Tax: Aligning ESG policy with Tax behavior, understanding and applying CSRD and Corporate Sustainability Due Diligence Directive (CSDDD), payment of appropriate global corporate taxes, process controls and compliance, assessing the total tax contribution.

This is a lot of information and new controls and reporting requirements that are being placed on companies. Companies may face difficulties with data collection and analysis, understanding reporting standards, resource constraints, and availability of reporting tools.

What is the key takeaway for companies?

- ESG is on the Board agenda.
- Tax should be pro-active in aligning to wider ESG initiatives.
- Conversations to be had can focus on:
  - o Be aware of country and multilateral legislation and initiatives that will impact their level of tax disclosure.
  - o Benchmark their tax disclosures to their industry and peers.
  - o Support the business in terms of internal governance and tax risk management.
  - o Ensure a culture of no surprises when it comes to tax risk and tax transparency.

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