

EU carbon tax: Government to shoulder 90 per cent compliance bill of MSMEs

The impact is likely to be felt the most by the iron and steel sector, where extent of decline in EU imports could be 24%

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The UK too has plans to impose its version of CBAM from 2027. (Reuters)

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The Centre is working on a scheme to absorb 90% of the compliance cost borne by micro, small, and medium enterprises (MSMEs) to help soften the disproportionate impact of the Carbon Border Adjustment Mechanism (CBAM) compliance burden imposed by the European Union, *The Indian Express* has learnt.

India's efforts to secure a concession for its small industries in negotiations with developed countries have not worked, and the industry has been seeking assistance to meet the steep annual compliance costs due to the imposition of the EU's carbon tax since January 1, 2026.

The UK too has plans to impose its version of CBAM from 2027. CBAM is an EU policy designed to put a price on the carbon emitted during the production of carbon-intensive goods that are entering the EU.

Complying with the regulation is seen as a major global challenge, as declarants must track the embedded emissions of their goods, including direct emissions and, for certain sectors such as cement and fertilisers, indirect emissions. Industry sources said that the compliance cost for each MSME unit to meet the requirement under carbon tax alone is Rs 15 lakh to 20 lakh and that they do not have the wherewithal to report the number of data points sought under the regulation by the EU.

India is the world's second-largest producer of both crude steel and primary aluminium.

Steeper challenge for MSMEs

An Indian exporter is required to submit CBAM certificates that correspond to the total embedded emissions. The regulation becomes a major challenge for MSMEs as the EU says that if exporters are unable to provide actual data, importers must use "default values" provided by the European Commission. The default values for CBAM goods have to be increased by a proportionately designed percentage 'mark-up' in their value.

"These mark-ups are 10% in 2026, 20% in 2027, and 30% from 2028 onwards. Default values, including mark-up, have been determined to ensure that embedded emissions are not underestimated when applying default values," the regulation said.

"For MSMEs, the principal challenge under CBAM is not necessarily the carbon levy itself, but the cost of compliance. Unlike large corporations, MSMEs often lack the technical expertise, systems and financial resources to measure, verify and report embedded emissions in accordance with CBAM requirements. They may have to incur significant upfront expenditure on carbon accounting, third-party verification, digital reporting systems and capacity building," Ayush A Mehrotra, Partner, Khaitan & Co said.

"These are largely fixed compliance costs, which means they do not reduce in proportion to the size of the business or export volumes.

"As a result, MSMEs bear a disproportionately higher compliance burden than larger exporters, potentially eroding their price competitiveness in the EU market. If these costs are not addressed

through targeted policy support, smaller exporters may find continued access to the EU market commercially unviable despite having competitive products,” Mehrotra said.

CBAM impact on India

Imports from India would decline for all CBAM commodities, and the impact of the CBAM is likely to be felt the most by the iron and steel (I&S) sector, where the extent of the decline in imports by the EU could be about 24%, and the Indian Council for Research on International Economic Relations (ICRIER) working paper released this month. The fertilisers and aluminium products, followed by metal products, are next in line. India’s global export of I&S will decline by 5.7%; for China, the corresponding estimate is 1.2%.

This reduction is primarily due to a reduction in exports to the European Union.

The report said that CBAM shall adversely impact India’s trade with the EU and will have a negligible effect on carbon emissions, adding that the impact level on carbon emissions is hard to determine and depends on the type of inputs used to produce the finished goods in the sector.

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