THE MISSING LINK IN CARBON BORDER GOVERNANCE: INDIA'S CARBON CREDIT TRADING SCHEME AND THE EU CBAM

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ABSTRACT

The Carbon Border Adjustment Mechanism of the European Union (EU) introduced a novel approach to decarbonization, which imposes a carbon cost on a certain category of imported goods in order to prevent carbon leakage. Despite the fact that the mechanism is designed to address climate change, it poses a significant threat to developing countries like India, which is currently forced to introduce a separate Carbon Credit Trading Scheme (CCTS) to reduce emissions. At the same time, India's efforts to meet the carbon neutrality goals are complicated by the fact that the EU does not recognize the carbon pricing mechanism introduced by the country. As a result, there is a considerable risk that Indian steel and aluminium producers may be subjected to double carbon pricing under the new regulations.

The current paper seeks to explore the potential trade and legal disputes between the EU and India for analyse how the EU's policies align with the foundational environmental treaties, including the General Agreement on Tariffs and Trade (GATT), the environmental provisions of GATT 1994, particularly the exceptions provided for in Article XX, and the principle of Common but Differentiated Responsibility (CBDR). In this regard, the analysis aims to demonstrate that the lack of appropriate procedure for the recognition of another jurisdiction's carbon pricing mechanism by the EU has become an integral weakness of the current system. Furthermore, the paper argues that recognizing the equivalence of India's domestic carbon pricing policies, to the extent of the similarities between the mechanisms, may provide a variable solution to the problem of double carbon pricing and facilitate the balance between environmental goals and trade interests of the developed and developing countries.

Keywords: CBAM, Carbon Credit Trading Scheme, India, European Union, GATT, CBDR, Carbon Pricing.

1. Introduction

Climate change has become one of the most pressing matters of the twenty-first century. Policies and regulations in different countries tend towards ensuring that there is less greenhouse gas emissions while still promoting economic development. The state's policies are increasingly prioritizing the obligation to reduce emissions, as well as the obligation not to let other countries off the hook for their emissions. Thus, carbon border measures emerged as a way to tie climate change and international trade together. The EU's Carbon Border Adjustment Mechanism (CBAM) is an explicit example of a measure designed to hold a country accountable for its greenhouse gas emissions. It has implications for the international trade of the countries which have a significant amount of exports to the EU. One of such implications is an upcoming conflict between the EU and India. The latter country has been making remarkable efforts recently in terms of carbon emissions reduction. Those efforts were rewarded by introducing the Carbon Credit Trading Scheme (CCTS) under Energy Conservation (Amendment) Act, 2022. The problem is that currently, India's efforts are not recognized by the EU in terms of the CBAM carbon price deduction. As a result, it may lead to extra carbon costs for India's firms that export to the EU. The discrepancy in carbon pricing regimes between India and the EU will affect the competitiveness of India's exports to the EU, which is especially acute for the steel and aluminium industries. This discrepancy and its effect on international trade relations is what this paper is about.

This paper focuses on the non-recognition of India's carbon credit trading scheme by the EU as a carbon pricing mechanism. The real issue with Europe’s new carbon import fee isn't its goal to fight climate change, but it's "my way or the highway" approach. The policy assumes that every country needs to copy Europe's exact system to count as environmentally friendly. This strict approach hits growing economies hard. That double charge isn't just unfair; it penalizes countries that are actively spending money to green their industries. Instead of forcing every trading partner to copy its rules word-for-word, Europe should look at the bigger picture: if a country's carbon system actually brings down emissions, it deserves proper credit at the border.

Additionally, it is argued that the absence of a comprehensive mechanism of recognition of other countries' carbon pricing mechanisms in the current EU's CBAM is the underlying factor. Thus, it can be stated on the basis of this paper that establishing recognition of India's

ECTC, where it passes the corresponding tests, would be an important step in balancing the principles of climate justice and international trade. It may also reduce the risk of double carbon pricing and, therefore, help prevent the emergence of a trade conflict between the world's largest economy and the fastest-growing one.

2. The Recognition Gap under the EU Carbon Border Adjustment Mechanism

2.1 India's Carbon Credit Trading Scheme

India has been developing its domestic carbon market through its Carbon Credit Trading Scheme. Energy Conservation (Amendment) Act, 2022, which provided the Central Government with the power to notify a framework for carbon credit, gave the necessary legislative backing to the scheme. The scheme's implementation has been underway since 2023, when the Ministry of Power started notifying rules (Press Information Bureau, 2023).

The scheme's compliance and offset mechanisms are overseen by two entities. The Bureau of Energy Efficiency monitors the carbon market, while the Central Electricity Regulatory Commission regulates the issue of Carbon Credit Certificates (Central Electricity Regulatory Commission, 2023).

India's Carbon Credit Trading Scheme consists of two mechanisms: *compliance and offset.* The compliance market focuses on heavy industrial emitters. It builds upon India's long-standing *Perform, Achieve, and Trade (PAT)* scheme which historically covered over 490 energy-intensive facilities by setting target greenhouse gas emission intensities across major manufacturing sectors, including steel, aluminium, cement, petroleum refineries, and petrochemicals. Facilities that perform better than their assigned targets earn carbon credit certificates, while those exceeding their emission baselines must buy credits on the market to meet their compliance obligations (Holzer, n.d., #).

Meanwhile, the offset mechanism encourages voluntary participation in the carbon market by allowing organisations to earn carbon credit certificates for reducing, capturing, or avoiding GHG emissions beyond the reductions required by the compliance mechanism. According to the government notification, there are nine offset areas, *including renewable energy, agriculture, forestry, waste, transport, construction, and carbon capture, utilisation, and storage*. India's domestic carbon market design is far from complete since only some sectors

and sources of emissions have been included in the current proposals. Nevertheless, the country has made significant strides towards building its carbon pricing architecture, exemplified by the carbon credit trading scheme (Shrivastava et al., n.d., #). Policies on carbon credit trading, implementing agencies, and even the sectors subject to the compliance mechanism have been developed. However, the domestic carbon market design is only one side of the coin, while the other is whether India's trading partners, the EU, will accept it, which they have not. Therefore, the next section will disclose details about the CBAM deduction procedure and explain why India's CCTS has not been recognised by the EU (Asian Development Bank, n.d., #).

The CCTS has been notified with the objective was to creating a financial incentive for GHG-emitting industries that reduce their emissions and impose a penalty on those that do not, which would allow transitioning to a low-carbon economy of reducing, removing, or avoiding greenhouse gas emissions from the Indian economy by pricing such emissions through the trading of Carbon Credit Certificates (Ministry of Power, 2026; Government of India, 2023). It aims to reduce the overall greenhouse gas intensity through a unified domestic trading system that addresses gaps in earlier regimes (Bureau of Energy Efficiency,

n.d.). The scheme is designed to create a credible, transparent compliance carbon market that embeds a price on emissions and turns decarbonisation into a financial opportunity rather than a cost burden (IEEFA, 2026).

The CCTS faces critical challenges. The most pressing is the lack of recognition by the EU for CBAM purposes—recognition requires product-level attribution, evidence of payment, and equivalence to the EU ETS, which are currently unmet (illuminem, 2025; pv magazine India, 2026). Domestically, the scheme excludes the power sector (~40% of national emissions), risks weak governance and low carbon prices (Climate Risk Horizons, 2026), and suffers from delays in notifying final targets. Moreover, the transition from PAT carries forward baggage of weak enforcement, inconsistent plant-level reporting, and poor verification, which threaten to replicate past market failures and dilute climate outcomes (IEEFA, 2026; pv magazine India, 2026).

2.2 CBAM Carbon Price Deduction Rules

The EU Carbon Border Adjustment Mechanism obliges importers to buy carbon emission allowances from the EU when importing certain goods, among which are steel, aluminium,

fertilizers, cement, and electricity. The new regulation was designed to prevent the carbon leakage and promote decarbonization, while not putting European industries at a disadvantage compared to those of the countries with less stringent climate policies. Reports suggest that the CBAM is one of the most ambitious initiatives in terms of connecting climate and trade, which took effect at the beginning of the current year.

At the same time, the regulation allows importers to deduct the amount of CBAM carbon emission allowances corresponding to the carbon price paid in the country of origin. Such a

deduction prevents double-counting of carbon emissions between the EU and the importing country. However, the deduction is only possible if the carbon pricing method used in the country of origin is acknowledged by the EU (International Carbon Action Partnership, n.d., #). Thus, the importers are obliged to provide evidence of the carbon price, emission calculation methodology, as well as monitoring and verification system used in the country of origin.

India has a carbon market, based on the CCTS, however, so far, its carbon pricing mechanism has not been recognized by the EU. Therefore, India's exporters are forced to buy CBAM allowances from the EU when exporting goods to the Common Market despite having carbon emission allowances. The analysis of the impact of the CBAM on India suggests that India's steel and aluminium industries will be especially hard-hit by the new regulations.

2.3 The Missing Link

Essentially, the entire discussion revolves around the recognition of carbon pricing, set by India. Both countries apply carbon pricing mechanisms; however, the issue is whether India's carbon pricing can be recognized as equivalent to that of the EU. India has made a big step towards a broader carbon market and carbon pricing-based economy, with the launch of the CCTS, however, there is no evidence that India's compliance system is eligible for carbon price deduction under the CBAM framework, according to which there is no information on the assessment procedure either.

The reason lies in a structural mismatch between what Article 9 requires and how CCTS operates. Article 9 recognizes a carbon price "effectively paid" — a tax, levy, fee, or emissions allowance surrendered under a mandatory, legally enforced scheme (Regulation (EU) 2023/956, 2023, Art. 9). The European Commission's draft implementing rules, published in

May 2026, sharpen this further by requiring that a qualifying scheme take the form of a mandatory tax, levy, or fee applied uniformly across a sector (European

Commission, 2026). Nor does the India–EU FTA close this gap: its carbon-cooperation annex extends a commitment to non-discriminatory treatment and future technical dialogue, but stops short of recognizing CCTS under Article 9 (Borderlex, 2026).

Steel, aluminium, and electricity industries are expected to bear the brunt of the new CBAM carbon price deduction rules, which require additional reporting and monitoring. Indeed, the missing link between India's carbon pricing and eligibility for carbon price deduction under the CBAM framework is a major setback for India's carbon market development. Recognition of India's compliance system by the EU could become a turning point in India's carbon market development, while the recognition of carbon credits generated by the offset system would be beneficial for both economies, as it would level the economic playing field to a certain extent.

3. Trade and Legal Conflict

The EU announced the introduction of the Carbon Border Adjustment Mechanism to achieve carbon neutrality. According to the new policy, the EU will impose duties on imported goods depending on the amount of emissions associated with them to ensure carbon competitiveness. However, the introduction of tariffs based on the amount of emissions entails several trade law issues, in particular, the problems associated with the emission reduction regimes of other countries. Although the EU's initiative brings significant benefits, it is essential to analyze the potential legal conflicts associated with it. First, it is critical to assess whether the EU policy complies with the WTO law. Second, the allocation of rights and responsibilities between different countries should be examined to determine whether the EU respects *the principle of common but differentiated responsibilities.*

3.1 CBAM and WTO Law Compatibility

The EU's CBAM represents the intersection of climate and trade policy. Its purpose is to ensure that carbon costs are not passed on to the EU through imports. It aims to impose the same carbon costs on certain goods as would apply to domestic production and to reduce the risk of carbon leakage. The definitive implementation of CBAM commenced on 1 January 2026 and will apply to steel, aluminium, cement, fertilisers, electricity and hydrogen. It allows for a

reduction in the CBAM amount where a carbon price has been paid in the country of origin, subject to certain conditions. India's CCTS has been established on a similar basis. It is hard to disagree with the desirability of reducing carbon emissions. The challenge is that carbon emissions are embedded in trade, and the imposition of a carbon tax inevitably raises questions of trade discrimination. The EU must therefore navigate between its climate objectives and its trade obligations under the WTO. The General Agreement on Tariffs and Trade (GATT) 1994 provides a useful framework for evaluating the compatibility of CBAM with WTO law. In particular, the relevance of Article I, II, III, XI, and XX is discussed below.

Article I of GATT contains the *Most Favoured Nation (MFN) principle*. In essence, this requires that a contracting party does not grant preferential treatment to the goods of one WTO member over another. This is relevant to CBAM because different countries have adopted different approaches to carbon pricing. Some have imposed a carbon tax, while others have established emissions trading schemes (ETS). A third category of nations has embarked on the development of carbon-credit trading schemes. The question therefore arises as to whether a differential application of CBAM would violate the MFN principle. This could happen if a carbon tax or ETS is applied to certain imports but not to others. Similarly, a discrepancy in the treatment of different carbon-pricing mechanisms could also give rise to an MFN issue. However, it would be wrong to conclude that the very fact of differential treatment violates the MFN principle. The EU must also consider whether it is reasonable to require imports subject to a carbon tax or ETS to demonstrate that a carbon price has been paid. In this context, it is important to distinguish between carbon-pricing mechanisms and the carbon costs actually incurred by producers. India's introduction of the CCTS is a prime example of a carbon-pricing mechanism that has been developed on a domestic basis. It does not follow the same model as the EU's ETS. However, this does not necessarily mean that the carbon costs embedded in Indian goods should be disregarded. The critical question is whether these costs can be demonstrated and taken into account (Zachmann & McWilliams, n.d., #).

Article II of GATT 1994 is the Schedules of Concessions provision. *It requires that a WTO member not impose ordinary customs duties on another member's goods in excess of the rates it has bound in its own tariff schedule*. It's fundamentally about tariff ceilings a country has committed to, not about whether duties are applied in a discriminatory or non-discriminatory manner. That's what Articles I (MFN) and III (National Treatment) govern instead, which is the distinction your draft was missing. There's one part of Article II that is directly relevant to

CBAM, though and it's more useful to your argument than the discrimination framing was. Article II:2(a) carves out an exception: a member may impose, at any time, "a charge equivalent to an internal tax" on an imported product, consistent with Article III (2), even if that charge would otherwise count against the bound tariff ceiling. This is the actual legal hook the EU is expected to rely on the argument that CBAM certificates aren't a customs duty at all, but a border-adjusted mirror of the EU ETS's internal carbon price, and therefore fall under this exception rather than counting against the EU's bound tariff commitments.

Under the CBAM, an adjustment is made where a carbon price has been paid in the country of origin. This is relevant to the discussion of MFN considerations. However, it also raises the issue of whether the carbon costs incurred by producers in the country of origin should be taken into account. In the context of India, the issue is not so much whether Indian producers have carbon credits, but whether the carbon costs incurred by them can be demonstrated and taken into account.

Article III deals with *National Treatment*. In essence, this means that imported goods must be treated no less favourably than domestic goods. This principle has particular relevance to CBAM. This is because the carbon costs associated with imported goods must be compared to the costs associated with domestic production. The EU contends that the imposition of CBAM is justified by the fact that domestic producers are already subject to carbon costs. However, the application of CBAM to imports may nevertheless violate the principle of National Treatment. The justification for CBAM rests on the proposition that domestic producers are subject to carbon costs. Therefore, they should not bear an unfair competitive disadvantage compared to foreign producers who do not incur similar costs. However, this argument fails to take account of the fact that some foreign producers already incur carbon costs. This is particularly relevant to India, which has implemented its own carbon-pricing mechanism. If Indian producers incur carbon costs that are similar to those incurred by EU producers, then it is hard to argue that they should be subject to additional costs under CBAM. The critical issue is whether the carbon costs incurred by Indian producers can be demonstrated and taken into account.

The relevance of Article XI is limited to the extent to which CBAM constitutes a quantitative restriction on imports. This is unlikely to be the case. By its very nature, a carbon tax does not impose a quantitative restriction on trade. It therefore *falls outside the scope of Article XI.*

The more relevant provisions of GATT are therefore I, II, and III, with reference also being made to Article XX.

As indicated above, CBAM is intended to serve an environmental purpose. *Article XX of GATT* contains various exceptions that apply *to measures of a trade-restrictive nature adopted for reasons of human health, animal and plant life, and the conservation of natural resources.* In particular, reference should be made to Article XX(b) and XX(g). These provisions apply to measures necessary to protect human life or health and to conserve exhaustible natural resources, respectively. The EU has the option of relying on either of these two exceptions. Climate change clearly falls within the scope of Article XX(g). The EU can therefore contend that CBAM is a legitimate measure for the conservation of natural resources. In addition, climate change also has an adverse impact on human health. This means that Article XX(b) also applies. It must nevertheless be borne in mind that invoking Article XX(g) does not automatically justify CBAM. This is because the language of Article XX(g) also requires that the measure should not be applied "in a manner that would constitute a disguised restriction on international trade". This means that the EU must demonstrate that the carbon costs associated with CBAM are justified and do not go beyond what is necessary to conserve natural resources. It must also demonstrate that the application of CBAM does not have an adverse impact on international trade.

The chapeau to Article XX is also relevant to the discussion. It states that the exceptions enumerated in Article XX shall be applied *"with due regard to the needs of developing countries"* and *"to the principle of mutual benefit"*. This means that the EU must demonstrate that CBAM is not being used to gain an unfair advantage over developing countries. The discussion turns back to the issue of whether the carbon costs incurred by Indian producers should be taken into account. The EU is free to impose carbon costs on imports, but it must demonstrate that these costs are comparable to the costs incurred by domestic producers. The purpose of CBAM is to ensure that carbon costs are passed on to importers. However, this should not mean that imported goods are subject to higher costs than goods produced in the EU. This brings us back to the question of whether the carbon costs incurred by Indian producers can be demonstrated and taken into account. This leads to a more general discussion of the principle of Common But Differentiated Responsibilities (CBDR). This principle reflects the fact that not all countries are in the same position when it comes to climate change. It is discussed further below in the context of India's climate policy.

3.2 Climate Justice: The Principle of Common But Differentiated Responsibilities

India's climate policy is based on the principle of CBDR. This principle reflects the fact that *not all countries are responsible for climate change to the same degree and that not all countries are in the same position to address the problem.* It is therefore important to distinguish between developed and developing countries. The principle of CBDR is straightforward. It recognises that all countries have a responsibility to address climate change, but it also reflects the fact that this responsibility is not the same for all countries. In essence, it is a recognition of the fact that developed countries have contributed disproportionately to the problem, while developing countries are likely to be more adversely affected by the impacts of climate change.

India has consistently advocated for the principle of CBDR, both within the WTO and in its bilateral relations with other countries. This does not mean that India is totally unresponsive to climate change. On the contrary, India has taken a number of measures to reduce its carbon emissions. It has also embarked on the development of a carbon market, which takes the form of the CCTS. India's primary concern is that its climate commitments should not come at the expense of its development objectives. This is where CBAM comes into the picture. India's concerns are similar to those of other developing countries, namely that climate policies adopted by developed countries will have an adverse impact on their trade competitiveness. The problem is exacerbated by the fact that CBAM applies to a wide range of inputs, including steel and aluminium. These are critical to India's economic development, but they are also extremely energy-intensive.

India's development strategy requires that it *transition to a more sustainable economic model.* This will inevitably entail significant costs, particularly in relation to energy. The imposition of CBAM will add to these costs, without necessarily contributing to India's climate objectives. This is because India already has its own carbon-pricing mechanism, namely the CCTS. Ideally, it would be preferable for the carbon costs embedded in Indian goods to be taken into account when calculating the carbon costs associated with CBAM. This leads to a discussion of the relevance of the principle of CBDR to India's climate policy. It is important to distinguish between India's climate commitments and its development needs. *The principle of CBDR recognises that developing countries are likely to bear a disproportionate burden if climate policies are imposed on a uniform basis.* This is precisely what is happening with CBAM.

Developing countries are being required to bear additional costs without any consideration being given to their domestic climate policies (Uddin, n.d., #).

It must also be recognised that the principle of CBDR is not an absolute defence against the imposition of CBAM. It is entirely legitimate for the EU to impose carbon costs on imports in order to deter carbon leakage. However, the principle of CBDR should serve as a useful reminder that developing countries will be adversely affected if climate policies are imposed on a uniform basis.

This brings us back to the discussion of whether the carbon costs incurred by India should be taken into account. It is important to distinguish between the principle of CBDR and the practical implications of CBAM. *The principle of CBDR does not mean that developing countries should be completely exempt from carbon costs.* However, it does mean that their climate commitments should be taken into account when imposing additional costs on their exports. India's establishment of the CCTS is therefore a positive development. It demonstrates that India is prepared to take responsibility for its climate commitments. However, it also highlights the fact that India's climate policy is likely to be affected by the climate policies of its trading partners. If the carbon costs embedded in Indian goods are not taken into account when calculating the carbon costs associated with CBAM, *Indian producers will be subject to additional costs.*

This raises the issue of whether developing countries will invest in the establishment of carbon-pricing mechanisms if their efforts are not taken into account by their trading partners. It also raises the question of whether developing countries will be forced to adopt the same carbon-pricing mechanisms as their trading partners in order to avoid additional costs. It is therefore important to distinguish between the principle of CBDR and the practical implications of CBAM. India has demonstrated that it is prepared to take responsibility for its climate commitments. However, it is also true to say that its efforts are being undermined by the unilateral imposition of climate policies by its trading partners.

The principle of CBDR should therefore serve as a useful guide to the development of India's climate policy. It should also be noted that the principle of CBDR does not apply to the EU's climate policy. The EU is a developed country and therefore bears a greater responsibility for climate change. This means that the EU cannot rely on the principle of CBDR to justify its climate commitments. However, it must nevertheless take account of the fact that developing

countries are likely to bear a disproportionate burden if climate policies are imposed on a uniform basis. In particular, it must take account of the fact that developing countries are likely to have to incur additional costs if they are unable to demonstrate that their domestic climate policies are comparable to those of the EU.

In essence, the principle of CBDR serves as a useful reminder that climate policies should not be imposed on a uniform basis. This is because different countries are likely to be affected by climate change to a different degree and have different capacities to address the problem. It is therefore important to take account of the principle of CBDR when designing climate policies, including measures such as CBAM.

4. Economic Impact on Indian Export Industries

India-EU trade is dominated by India's exports of steel, aluminium, and other metals. The primary challenge derives from the fact that India's energy structure is heavily coal-dependent, meaning that domestic metallurgy is more energy and emission-intensive as compared to the EU.

India has set ambitious carbon-neutrality goals in line with its climate action plan, updated in 2022. In particular, *India pledged to reduce greenhouse gas (GHG) emissions from its economy by 45% on a per unit of gross domestic product (GDP) basis and 50% of electricity generated from non-fossil fuels by 2030 over 2005 levels*. *By 2035, India's emissions are to be brought down by 47% on a per GDP basis and 50% of electricity is to be produced by non-fossil fuels by 2035.* India's forests are estimated to absorb 3.5 to 4 billion tonnes of carbon dioxide equivalent (International Monetary Fund, n.d., #).

India has set the target of decarbonizing its economy in line with its climate action plan, however, it requires a lengthy policy implementation process and extensive investments. Until then, carbon pricing at the border will make India's emission-intensive production more costly and, consequently, less competitive as compared to domestic alternatives, *which will negatively impact Indian metallurgy,* in particular, and other emission-intensive industries, in general.

4.1 Economic Impact on Steel and Aluminium Industries

India is one of the biggest producers and exporters of steel and aluminium in the world; therefore, the introduction of a CBAM poses a serious threat to its steel and aluminium

manufacturing industries, as their products will become more expensive in the EU, making them less competitive. In addition, domestic metallurgy will have to buy carbon credits to offset its emissions. India's energy efficiency standards for large energy-intensive installations in sectors such as steel, aluminium, cement, refineries, petrochemicals, chlor-alkali, paper, and textiles are established by the Bureau of Energy Efficiency. As a result, energy-intensive industries will incur significant costs for installing new technologies in line with India's energy and carbon neutrality goals under the Carbon Credit Trading Scheme. India's carbon pricing mechanism for carbon emission-intensive sectors is in line with its climate goals, international obligations, and energy security. Still, it should be noted that India's Carbon Market Mechanism may interfere with India's trade in certain goods. First, CBAM targets specific goods, in particular, steel, aluminium, cement, fertilizers, electricity, and hydrogen. Second, *it is not clear how the EU factors in India's domestic carbon pricing on the import of the said goods*; until then, Indian steel manufacturers will have to incur additional costs of India's domestic carbon pricing mechanism making them subject to double penalty (International Energy Agency, n.d., #).

4.2 Effect on India's exports competitiveness

While the imposition of additional carbon charges will raise the production costs for the exporters, they will also have to undertake additional measures to measure and monitor the carbon emissions from their production processes in compliance with the EU directives. Therefore, the exporters may also have to bear additional costs in terms of professional expertise to measure and monitor the carbon emissions for firms, which will further raise their production costs, affecting their competitiveness in the international market. While the large firms may be able to absorb these additional costs with relative ease, the small firms may not be able to do so. Moreover, the Carbon Credit Trading Scheme in India still needs to gain credence in the EU carbon price deduction mechanism. In other words, Indian exporters may have to bear additional carbon taxes to comply with the local and foreign laws. The reports indicate that steel, aluminium, cement, and fertilizers are some of the economic sectors in India that will be highly vulnerable to the introduction of the Carbon Border Adjustment Mechanism. These sectors will not only have to bear additional carbon taxation but will also have to comply with the monitoring and evaluation framework required by the EU while measuring carbon emissions. While the additional carbon taxation component will offset some of the production costs for these firms, they will still be required to bear additional costs in terms of updated

monitoring and evaluation framework, making them highly vulnerable to additional production costs (European Parliament and Council of the European Union, n.d., #).

While the Carbon Border Adjustment Mechanism will be overall detrimental to most of the firms in terms of additional production costs, some firms are considering this as an opportunity to invest in more sustainable production technologies and consequently reduce their carbon footprints while also making themselves competitive in the international market. Firms are already making investments in cleaner technologies and alternative sources of energy to reduce their carbon emissions and comply with the Carbon Border Adjustment Mechanism. These investments in most of the firms, however, will not only make them sustainable but also competitive if the Carbon Credit Trading Scheme becomes credible in other international markets.

4.3 The Disproportionate Burden on MSMEs

While large exporters can absorb CBAM's reporting and certification costs, India's micro, small, and medium steel and aluminium enterprises face a structurally different problem: *most lack the technical capacity to generate the emissions data CBAM demands from their own supply chains*. Industry representatives have described the compliance standard as disproportionate, noting that a workshop employing fifteen workers must meet the same emissions reporting standard as a billion-dollar steelmaker (Kumar, 2026). This is not a hypothetical concern — the first wave of shipment seizures and order cancellations at European ports, triggered by missing compliance reports, began within weeks of CBAM's definitive phase taking effect in January 2026 (Kumar, 2026). The Indian government has responded by considering a scheme to bear 90 percent of MSME compliance costs (Business Standard, 2026), but this addresses the cost of compliance without resolving the underlying non-recognition problem: even a fully CBAM-compliant MSME exporter gains nothing from its CCTS participation, since that scheme's credits are not deductible under Article 9. The burden therefore falls hardest precisely on the exporters least equipped to absorb it.

5. The Geopolitics of Carbon Pricing: India's Diplomatic Leverage

5.1 Bilateral Leverage: The EU–India FTA as an Unfinished Bridge

The India-EU summit held on 27 January 2026 at the 16th meeting of the two sides

concluded the FTA negotiations with CBAM being described as one of the most negotiated items of the deal (Apparel Policy News India, 2026; Borderlex, 2026). The deal fell short of the blanket CBAM exemption that India had sought but did secure a CBAM annexure with a "forward-looking most-favoured-nation assurance" — any future CBAM flexibility granted by the EU to other countries will automatically be extended to India and a joint climate-action platform backed by €500 million in EU support (Argus Media, 2026). This should be viewed as a bridge not yet completed rather than a failure. Article 9 of the CBAM Regulation obliges the EU to provide a methodology for the effective offset of carbon prices paid abroad; if CCTS can be harmonized with that methodology, India retains CBAM-equivalent revenue domestically (IntLawGrrls, 2026). The FTA does not get this recognition by default, but its "technical dialog" route keeps the door open for further negotiation.

5.2 Multilateral Pressure: Coalition-Building with the Global South

In addition to bilateral leverage, India has sought to build coalitions with other similarly exposed developing economies. As early as April 2021, the BASIC group (Brazil, South Africa, India, China) called CBAM discriminatory and has since pushed to place it on the COP agenda (GMK Center, 2026). Recent proposals include India building coalition architecture through BASIC and the WTO developing-country caucus using forums such as the WTO Ministerial Conferences and BRICS climate-finance coordination (Down To Earth, 2026). This is important because it reframes non-recognition from a bilateral dispute into a structural grievance of a bloc of developing economies — a position as a bloc that has more procedural heft, especially given the chapeau requirement of GATT Article XX that CBAM not amount to "arbitrary or unjustifiable discrimination." The BASIC group and the wider Global South coalition ensure that India does not negotiate in isolation but rather talks as a member of a group whose total trade exposure forces the EU to establish a general recognition framework rather than bringing legal action against each country's carbon-pricing system individually.

6. Recommendations

6.1 A Transparent Framework for Recognising Foreign Carbon Markets

The EU should establish clear, published criteria for assessing whether a third-country carbon

pricing mechanism qualifies for Article 9 deduction, rather than leaving recognition to be inferred case by case. These criteria should be objective and evaluable — legislative formalisation, institutional oversight, monitoring reliability, and verifiable emissions reduction rather than requiring structural identity with the EU ETS. Ideally, such criteria would be developed with reference to broader international benchmarks, potentially coordinated through the WTO or UNFCCC, so that recognition standards are not solely an EU-defined test applied unilaterally to trading partners (CEEW, 2025).

6.2 Gradual Rather Than Immediate Recognition

Recognition should be phased rather than binary. An initial, limited recognition of CCTS covering, for instance, its compliance mechanism before its offset mechanism would allow India to consolidate its carbon market's institutional maturity while still gaining partial relief from CBAM's certificate obligations. This avoids forcing developing economies to align their carbon pricing architecture with EU standards immediately, which neither their institutional capacity nor their development trajectory may support.

6.3 A Permanent India–EU Carbon Dialogue Mechanism

Beyond the technical dialogue already contemplated in the India–EU FTA's carbon-cooperation annex, both sides should establish a standing joint working group of officials, technical experts, and industry representatives to address carbon accounting, monitoring, and verification methodology on an ongoing basis. A permanent mechanism, rather than periodic political engagement, would allow the two sides to resolve technical disagreements such as whether CCTS certificates satisfy the "effectively paid" standard — through sustained expert dialogue rather than one-off negotiation.

6.4 Periodic Reassessment of Recognition Status

Recognition, once granted, should not be static. A periodic review mechanism would allow India to reapply for expanded recognition as CCTS matures for example, as its MRV standards strengthen or its offset mechanism gains credibility — while also giving the EU a structured basis for revisiting recognition if standards are not maintained. This creates an incentive structure that rewards continued institutional investment rather than treating recognition as a one-time determination.

6.5 A Transition Period with Technical Support

Given the acknowledged capacity constraints facing Indian exporters, particularly MSMEs, in meeting CBAM's monitoring and reporting requirements, a transition period paired with EU technical assistance on carbon accounting and verification capacity-building would ease the compliance burden during CCTS's institutional consolidation. This need not delay CBAM's core objective; it would instead ensure that the mechanism does not penalise exporters for structural gaps outside their control while recognition frameworks are being built.

7. Conclusion

The purpose of this paper was to identify the reason why India, which has its carbon market, is not considered by the EU for the implementation of the Carbon Border Adjustment Mechanism (CBAM). By analyzing legislation, reports, and other information on the topic, this research has found substantial evidence that India has made significant efforts to achieve carbon neutrality and has introduced its Carbon Credit Trading Scheme that covers numerous sectors. Nonetheless, this paper has shown that no clear pathway currently exists for integrating India's carbon market with CBAM, nor for structuring a broader recognition relationship between the two regimes. Both sides stand to lose from this unresolved gap: India's steel and aluminium producers, among the first to join the country's domestic carbon market, must now absorb the cost of adjusting to CBAM's requirements without credit for that participation, while the EU's own credibility on carbon border governance depends on CBAM being seen as a fair mechanism rather than a unilateral one — a perception that puts pressure on its broader economic partnerships with developing economies. Therefore, it is natural that India, as well as other countries that have opted for the development of their own carbon market, do not intend to follow the example of the EU Each country will choose for itself the method that it finds most effective, such as introducing a carbon tax, and will create its own carbon market, which will be similar to the Indian one. Thus, it is necessary to acknowledge the efforts of countries that have opted for participation in the CBAM pilot program and carbon neutrality in general. This paper does not advocate for the cancellation of the CBAM; instead, it should be adjusted so that the carbon emissions of all countries involved in the program are accurately accounted for and reduced.

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