



How to advocate for fair and effective EU carbon markets

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Executive summary

The EU Emission Trading System (EU ETS) is a central pillar of EU climate policy. It aims to reduce greenhouse gas emissions by putting a price on CO₂, operationalising the polluter pays principle, while generating revenue to support the energy transition. The system currently covers power generation, industry, aviation and maritime transport (ETS1) and will be extended to emissions from buildings and road transport through a second system (ETS2), due to enter into force in 2028.

The EU ETS is far from perfect. It has notable shortcomings that must continue to be addressed and improved to deliver on both its environmental and social objectives. Yet after 20 years of existence, it has also proven its efficacy and clear potential. Over time, successive revisions have strengthened the system, making it more robust. Emissions in ETS1-covered sectors have declined by 51% since 2005. At the same time, the system has generated substantial revenues, €39.8bn in 2024 alone, creating a significant opportunity to finance climate action and support for households and industry during the transition.

But while emissions have fallen overall, progress remains uneven across sectors. Industrial emissions, still heavily covered by free allowances, are stagnating, aviation emissions are increasing, and emissions from road transport and buildings have proven particularly difficult to reduce. These trends underline both the importance of continuing to improve ETS1 and the necessity of effectively implementing ETS2 to tackle emissions where they have so far been most persistent. The priority now is not to weaken the system, but to build on its progress.

At a moment when climate change is already hitting people hard, through more frequent and intense floods, droughts and heatwaves, the need for effective climate policy has never been clearer. Adding to that a context of energy price volatility and geopolitical uncertainty, accelerating the shift away from fossil fuels is not only a climate imperative but also an economic and security priority. By making pollution more expensive, and clean alternatives more competitive, the EU ETS can help drive investment into renewables, energy efficiency and industrial transformation, while providing revenues that can help make the transition affordable to households.

Yet the EU ETS is facing increasing political pressure. As ETS1 is set to be revised in 2026 and ETS2 is approaching its 2028 launch, there is a real risk of backsliding. Calls for simplification, competitiveness and short-term relief risk weakening the system at precisely the moment when it needs to deliver more. This guide outlines critical policy recommendations ahead of the review of ETS1 and on ETS2 implementation. This advocacy guide includes practical tools to assist civil society allies, including key narratives and messages, strategic advocacy moments, a timeline, main stakeholders involved in the policy-making process, and key readings and resources.

The task ahead is to continue improving the EU ETS: strengthening its environmental integrity, supporting investment in a competitive low-carbon economy, and ensuring it delivers both emissions reductions and a fair transition.

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List of acronyms

EU ETS – EU Emission Trading System (covers both ETS1 and ETS2)

ETS1 – Emission Trading System covering industrial, energy production, aviation and shipping sectors

ETS2 – Emission Trading System covering road transport and buildings

SCF – Social Climate Fund

SCP – Social Climate Plan

MSR1 – Market Stability Reserve of ETS1

MSR2 – Market Stability Reserve of ETS2

LRF – Linear Reduction Factor

CDR – Carbon dioxide removals

CRCF – Carbon Removals and Carbon Farming Regulation

RED – Renewable Energy Directive

EED – Energy Efficiency Directive

EPBD – Energy Performance of Buildings Directive

Introduction

The EU Emissions Trading System (EU ETS) is often referred to as the cornerstone of EU climate policy. The EU ETS is first and foremost an instrument designed to make cost-effective emission reductions, by creating a carbon market that applies a monetary value to greenhouse gases (i.e. putting a price on pollution that causes climate change). Revenues generated by the scheme can then be used to fund climate action. EU ETS covers two carbon pricing schemes: the Emissions Trading System for power, industry, aviation and maritime sectors (ETS1), and the Emission Trading System for road transport and buildings (ETS2). The scope of EU ETS was extended in the most recent ETS revision, of 2023, to include coverage of certain maritime sector emissions in ETS1, and the new ETS2 scheme was created.

Climate policy is facing pushback and EU ETS is no exception. As ETS1 will undergo its next scheduled review in 2026 and ETS2 is soon to launch in 2028, critical voices are getting louder. However, civil society and progressive industry alike are standing up for both ETS1 and ETS2.

The EU ETS is far from perfect but it is working. Now is not the moment to backslide on the impressive regulatory achievement that is the EU ETS. Rather, we need to improve the system.

This advocacy guide outlines why fair and effective carbon pricing is crucial and presents key policy recommendations to enhance aspects of social fairness, environmental effectiveness and public acceptance of ETS1 and ETS2. To support strategic advocacy efforts, the guide also provides key narratives and messages, strategic advocacy moments and timelines, identifies the main stakeholders involved in the policy-making process and lists key readings and resources.

Why does the EU have carbon pricing schemes?

1. Climate change is happening now

The climate crisis is already hitting people hard – consequences are experienced especially in developing countries but it is also affecting us in the EU. Hazards such as flooding, droughts, and heatwaves are becoming more intense, prolonged, and frequent, posing serious health and economic risks. Climate action might come with a cost, but climate inaction is far more costly. A 2026 study published in the Quarterly Journal of Economics confirms that

following current patterns, global warming will lead to a welfare loss of more than 30% and a social cost of carbon over \$1200 per tonne: numbers indicating that decarbonisation policies are by design cost-effective in large economies. Tackling the climate crisis has multiple other additional benefits such as on health and reducing vulnerability to fossil fuel price volatility, as well as greater geopolitical resilience.

2. Combat emissions from high-polluting sectors

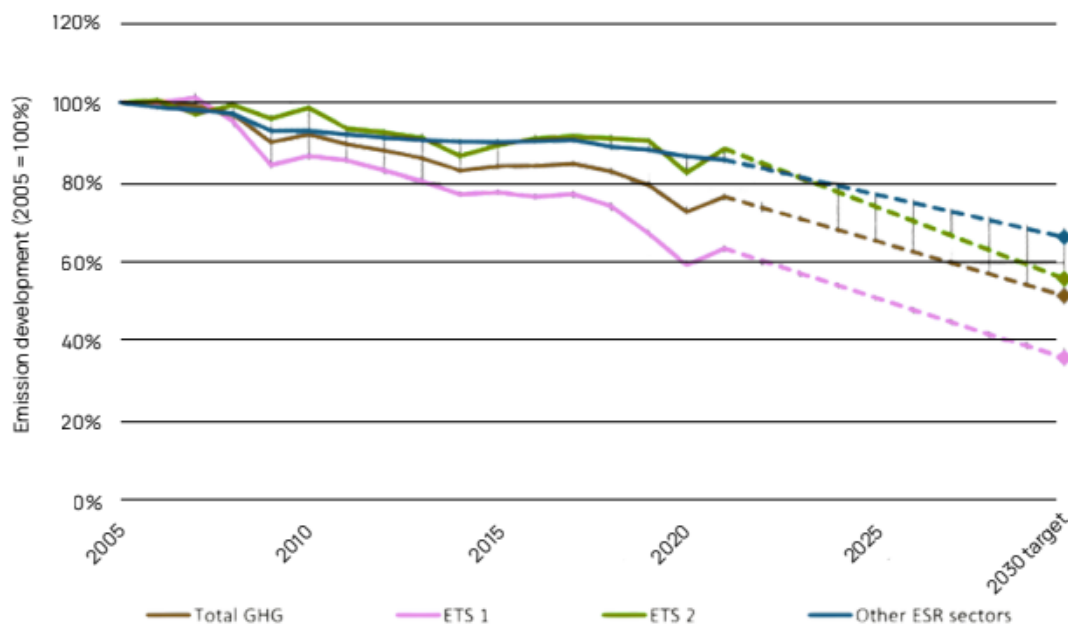
Between 2005 and 2024, emissions covered by ETS1 have declined by 51%, reflecting the effectiveness of carbon pricing as a means to drive decarbonisation. A lot of work, however, remains. Emissions from industry installations are stagnating, European airline emissions increased by 8% between 2023 and 2024, and continued to increase in 2024. Both aviation and maritime emissions are projected to increase further. While power sector emissions have decreased rapidly over the two most recent decades, the power sector still emitted 250 million tonnes of CO₂ from coal in 2025.

CO₂ emissions from road transport have also been slow to decrease over recent years, with member states struggling to implement effective regulations and instruments to cut

emissions. This was a key factor for the introduction of ETS2, which will also help increase the pressure on member states to invest in the complementary policies necessary to lower emissions in tandem with ETS2.

Road transport emissions account for the largest share of greenhouse gases from the broader transport sector, accounting for 73% in 2023, a share largely unchanged since 1990. In that time, car numbers have risen steadily and growth in both passenger and freight activity continues to drive emissions despite improvements in the energy efficiency of vehicles. CO₂ emissions in buildings account for one third of the EU's energy-related emissions and have fallen by 43% between 2005 and 2023.

Figure 1. Emission development since 2005 and 2030 target (EU27)



Source: Oeko-Institute with data from EEA (2023a)

3. Put a price on pollution to drive decarbonisation

By applying a price on CO₂, the EU ETS ensures that the polluter-pays principle, enshrined in the Treaty on the Functioning of the EU, is applied, making those responsible for emissions (rather than society at large) bear the costs. The EU ETS positively influences the development of a strong and certain investment signal that will increase the price of pollution as the market matures and the system – which operates a cap and trade principle – makes fewer pollution permits available as the cap shrinks. This will provide industry and people with the information necessary to invest in lowering their emissions today as a sensible long-term and cost effective strategy for the future.

Pricing pollution works: over the last 20 years, ETS1 has helped cut emissions from its sectors in half.

However, with the advent of ETS2, carbon pricing will become more noticeable, not only for industry but also for citizens who will have to pay for considerably more of their pollution, as the fossil fuel suppliers that are regulated by ETS2 will pass on the cost to end-users. To ensure a socially fair implementation of ETS2, it's imperative that vulnerable households that may be more affected by ETS2 prices receive targeted support to switch to clean heating and transport alternatives.

4. Create funding for climate action

The EU ETS is an important source of climate finance. While the fundamental aim of the EU's carbon pricing schemes is to reduce emissions, it has the co-benefit of generating hundreds of billions in revenue through the auctioning of emission allowances, which could be improved further should 90% of allowances no longer be handed out to industry for free. Appropriate spending of carbon pricing revenues offers a huge opportunity to finance climate action and to support people through the climate

transition. Out of all ETS2 revenues, €65 billion has been earmarked for the Social Climate Fund, which was embedded into ETS2, with the specific purpose of cushioning any negative socio-economic impacts caused by ETS2 on vulnerable households. The SCF is the first EU fund developed with the explicit purpose of alleviating energy and transport poverty but its size must be increased to make sure that it is fit for purpose.

5. Break free from fossil fuels

The EU ETS can play a significant role in boosting Europe's energy security by accelerating a reduction in the bloc's dependency on foreign imported fossil fuels by making them more expensive, while also strengthening the case for energy efficiency and domestic renewables. Recent energy crises have highlighted Europe's reliance on volatile fossil fuel markets, exposing households and businesses to sudden price shocks. Reducing this dependency not only stabilises costs but also reinforces the EU's sovereignty and resilience in the face of

geopolitical risks.

The International Energy Agency estimates that European households saved €100 billion between 2021 and 2023, thanks to additional renewable energy installations replacing expensive fossil fuels, following Russia's invasion of Ukraine. As long as Europe remains reliant on fossil fuels, high prices will disproportionately impact low-income households, who spend a larger share of their incomes on energy bills.

6. EU ETS inspires global climate action

The EU ETS is a leading international example of an effective climate policy, inspiring the development of an increasing number of carbon pricing schemes worldwide. In 2025, the World Bank estimated that more than a quarter of global emissions are covered by carbon pricing, raising \$100 billion in revenues in 2024 (of which the EU ETS raised €38.8 billion). Major trading partners (including China, South Korea, Japan, Turkey, and Brazil) have already implemented, or are

in the process of implementing, carbon pricing schemes. Complemented by the Carbon Border Adjustment Mechanism (CBAM) the EU ETS is ensuring an equivalent carbon price is paid by EU producers and importers, for selected sectors – which has incentivised other jurisdictions to make carbon polluters pay and hold on to the generated carbon pricing revenues to fund domestic decarbonisation, rather than paying them to the EU.

The EU ETS political landscape

ETS1

In the summer of 2026, the Commission is expected to launch a scheduled ETS1 revision – kick-starting a long negotiation process on the future of the carbon pricing system. The outcome of all previous revisions has been a more environmentally effective and ambitious EU ETS. However, European Parliament and national elections have changed the political dynamic and climate policy has found itself on the chopping block. ETS1 is at risk, and this is the first revision that could lead to backsliding of the bloc's cornerstone climate policy.

Policymakers and energy-intensive industries are calling for a retrograde approach in the name of competitiveness and regulatory deregulation, labelled as simplification (e.g. the Antwerp call to Alden Biesen). There has been intense pressure from several European governments, including Slovakia and the Czech Republic, as well as Italy, which has openly called for a suspension of the system. The results of this pressure can already be seen: in April, the Commission tabled an early review of the Market Stability Reserve (MSR1), that will do little to alleviate competitiveness concerns but risks prolonging serious climate damage into the 2030s. In the aviation sector, industry has pushed back on expanding the coverage of carbon pricing, and on tackling the sector's substantial non-CO₂ emissions, even resisting gathering data on it. Some prominent third countries are also becoming involved and are pressuring the EU not to price the pollution from flights that leave or land outside the EU.

Be it from industry or aviation, the pushback against ETS1 is misguided. It is clear that climate and industrial policymaking can and should go hand in hand. ETS1 has solutions to offer that can both drive and support industrial decarbonisation in a predictable and effective manner. Weakening the system now risks penalising businesses that are at the forefront of decarbonising their operations. We need predictable investment signals rather than political interference. Vocal support for the ETS1 is growing louder and emerging from all corners – from civil society to governments, companies and industrial associations.

ETS2

ETS2 is facing significant resistance, and many member states are severely delayed in implementing the system. ETS2 was only agreed upon in 2023, but policymakers have already intervened to weaken it, even before it gets up and running. The system, which was initially set to start in 2027, was delayed by one-year, as part of the horse-trading in the context of November 2025's 2040 climate target negotiations. The delay will result in around €50 billion in forgone auctioning revenues for climate investments and postponed climate action.

Under pressure from member states, the Commission also suggested changes to the Market Stability Reserve of ETS2 (MSR2) to lower the ETS2 price. The trade-off is that emissions under the system will increase by up to 600 million tonnes.

The ETS2 is not within the scope of the 2026 EU ETS review, but opponents are likely to try to (ab)use the opportunity to further weaken the system. The constant tinkering with the system must stop, and any changes to ETS2 must wait until the scheduled ETS2 review in 2028.

Similar to ETS1, competitiveness and simplification are presented as key arguments to weaken the instrument. In contrast to ETS1, another common concern cited by opponents and critics is the system's potential negative socio-economic impact due to the price added to energy bills.

While this is a valid concern, the response should not be to weaken the system, but rather to increase support for vulnerable households. The Social Climate Fund (financed by ETS2 revenues)

was established alongside the ETS2 exactly to cushion negative social impacts stemming from ETS2. There is an inbuilt solidarity mechanism in the SCF: member states with a higher need will receive proportionately more funding than the ETS2 price they pay. The fund, however, must be expanded in size and extended beyond 2032 to be fit for purpose. To access the fund, member states need to submit National Social Climate Plans, outlining how they will use the money, but at the time of writing, only a couple of plans have been submitted, long overdue for the requested deadline of June 30 2025. On top of this, member states should implement additional measures and social policy to further support vulnerable households, for example, those in rented accommodation. Climate and social policy can and should work in tandem.



Key recommendations for a fair and effective EU ETS

The policy recommendations cover actions to improve the fairness and effectiveness of both ETS1 and ETS2. The first 10 points are policy recommendations for the 2026 ETS1 review (ETS2 is not in the scope of this revision).

These are followed by 5 policy recommendations to ensure a fair and effective ETS2 implementation as well as measures that should be considered in the 2028 ETS2 review.

Policy recommendations for the ETS1 review

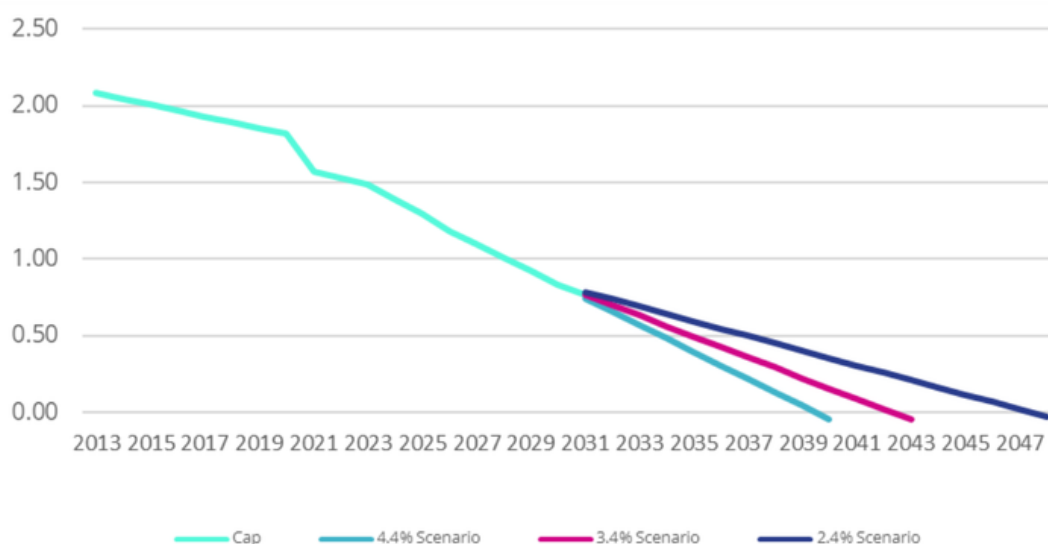
1. Want a new cap? Make it carbon budget neutral

The cap sets the total volume of emissions allowed under the ETS1 and sets the path of the declining trajectory necessary for the EU to stay within its remaining carbon budget. The pace of this reduction directly determines the level of climate ambition. The EU has committed to climate neutrality by 2050, with a milestone of net-90% emissions reductions by 2040, leaving limited room for a business-as-usual approach to emissions in ETS1-covered sectors.

The ETS1 carbon budget is largely set by three tools: the cap on annual emissions, the Linear Reduction Factor (LRF), which forces the cap down year after year to ensure increasing scarcity over time, and the Market Stability Reserve (MSR1), which removes excess allowances from the market. Together, these mechanisms provide predictability and underpin the system's credibility. Any modifications to this framework must be approached with extreme caution, as tweaking any of these levers can undermine both the environmental effectiveness of the ETS and investors' confidence in the system. In the short term, there is no need to tinker with the cap, the LRF, or the MSR1. If industry finally starts to decarbonise appropriately, then the ETS1 will remain oversupplied until 2036.

Any increase in the supply of allowances in the short term will either need to be cleaned up by the MSR1 later, or the EU's overall emissions will increase. Higher supply of allowances in the ETS1 has to be compensated by a greater effort to reduce emissions in non-ETS sectors, especially from agriculture – or climate targets will become unattainable.

Minor alterations to the LRF have significant impacts on the quantity of emission allowances available over time. Reducing the LRF to 3.4% would delay zero emissions until 2043, effectively allowing an additional one billion tonnes of greenhouse gas emissions into the atmosphere. A further reduction to 2.4% would push near-zero emissions out to 2048, resulting in roughly three billion additional tonnes of CO₂.



Sources: EC, CMW own calculations.

Looking beyond 2035, some very limited emissions may remain in certain industrial and international transport sectors, which might require adjustments to the cap trajectory and LRF. However, these residual emissions must be strictly defined and quantified as those that are left over after all abatement options have been used. They must exclude any fossil fuel emissions, or process emissions that can be captured and stored and should be limited to activities considered to be 'desirable' or too important for society to give up despite their climate impacts. Importantly, a residual emissions cap must continue to decline over time and be integrated into a broader trajectory towards net-negative emissions.

2. Use revenues wisely: kick out fossil fuels subsidies

Between 2026 and 2030, the ETS1 is expected to raise between €120 and 150 billion¹ in auctioning revenues for member states. On top of that, ETS1 revenues feeding the Innovation Fund and Modernisation Fund may increase the direct funding available for climate action by as much as €93 billion cumulatively.

These revenues need to be spent urgently and strategically with a clear focus on maximising direct emission reductions, supporting people most affected by the energy transition, and preparing against the impacts of the climate crisis itself. At the same time, the EU's international climate finance commitments need to be stepped up to meet the needs of the most vulnerable developing countries.

The list of climate-related funding priorities is outdated and needs a fundamental overhaul. Clearer safeguards and criteria on how member states spend ETS1 revenues are necessary to ensure they are not used to support fossil fuels subsidies or other unsustainable practices. Given the scale of needs and limited resources, spending must prioritise measures that deliver the greatest public value and avoid locking in unsustainable pathways.

Industry groups are hoping to claim these revenues to cover their own decarbonisation costs and extra subsidies (such as using the indirect cost compensation mechanism to compensate for the carbon cost of electricity use, even when fossil fuel-based), with little consideration for the broader societal needs. However, the climate impacts from industrial emissions are a burden for everyone, so there is no justification for ETS to be a mere 'cashback' tool for industry. Successful industrial transformation will require investment from both private and public sources.

The establishment of the Industrial Decarbonisation Bank would be a welcome development, but corporate polluters must not be the only beneficiaries of ETS1 revenues. Any public support to industry must be on the strict condition that climate spending can only be awarded if it is tied to a credible and enforceable decarbonisation plan, alongside social safeguards for workers. Without stronger conditionalities, public funds risk delaying rather than driving the transition.

¹ Assuming an EUA price range of €75 to €95.

3. Freebies have prevented investments: eliminate them once and for all

Free allowances were introduced as a temporary measure to protect industry from the phantom of carbon leakage. Two decades later, they remain widespread, still covering around 90% of industrial emissions. The scale of the support is staggering: between 2008 and 2021, about €200 billion worth of EUAs were handed out at no cost to heavy industry; these allowances were surrendered, banked, or even sold for a profit. In 2024 alone, nearly 500 million allowances were handed out for free at a value of over €32 billion. These are foregone revenues that member states won't be able to spend on climate action, on supporting vulnerable people, or on the transformation of the European economy.

The Court of Auditors confirmed that free allocation hampers decarbonisation efforts. Emissions from electricity and heat generation, which do not receive free allowances, decreased by 28.6% between 2013 and 2022 after their free allowances were phased out, whereas industrial emissions decreased by less than 9%.

From the outset, free allowances were always meant as a temporary measure, yet the vested financial interest they have created has led to their repeated extension. This must now come to an end. The planned phase-out trajectory for CBAM products should be respected and remaining freebies awarded to non-CBAM ETS1 sectors that the European Commission deems at risk of carbon leakage (with refineries and chemical products the largest polluters of that group). These must be phased out fully by 2034 at the latest and covered by CBAM instead.

As long as free allowances remain available to industrial sectors, their allocation must only be made on the strict condition that they are disbursed where additional decarbonisation investments of equal value can be proven, similarly to what has been proposed in the Temporary Decarbonisation Fund. Conditional free allocation based on energy efficiency audits and climate neutrality plans must be strengthened by ensuring the transparency, public accessibility and enforceability of the plans. Without such conditions, public support will continue to finance shareholder payouts rather than a decarbonisation transition (from 2010 to 2023, European firms that should be investing in their energy transition generated €2.1 trillion in net profit and distributed €1.6 trillion to shareholders)

After two decades of free pollution and missed opportunities, the EU cannot continue to subsidise polluters with impunity. Industrial air pollution in the EU generates €268-428 billion in health and environmental damage every year: someone has to pay that bill. Until now, it has been paid for by society while the industry profits. With the implementation of ETS2 for road transport and buildings, ordinary Europeans will pay the full price of their emissions; the same principle must now apply to industry. Any future support must address societal needs, not just reflect industry pressure.

4. Predictability is good for business, allow the MSR1 to do its job

The Market Stability Reserve (MSR1) is one of the Emission Trading System's most powerful mechanisms. In its current set-up, it has not only resulted in measurable climate benefits but has also averted a carbon price collapse. Since its establishment, the MSR1 has successfully invalidated 3.4 billion ETS1 allowances, preventing the equivalent number of tonnes of CO₂ from entering the atmosphere. It has done this by swallowing excess allowances directly from the market, and by cancelling out surplus from the reserve supply that exceeded its maximum threshold of 400 million allowances. The market is forecast to become short in 2035, at which point MSR1 will start releasing 100 million allowances per year into the ETS1 to cover actual emissions.

This issue highlights how ETS1 is still plagued by the problem of structural oversupply as the availability of allowances continues to outstrip demand: a problem that will persist at least until 2031. In 2024, supply was 227 million tonnes above demand due to an overly generous cap. The dilution of the MSR1, as would be the case should the proposal of deleting the invalidation mechanism be approved, risks fundamentally upsetting the market's supply-and-demand balance. This will unduly inflate greenhouse gas emissions after 2030, hindering the EU from achieving its 2040 climate target. Moreover, it risks weakening the long-term carbon price signal, undermining the business case for the deep decarbonisation investments that must be undertaken already today.

5. An absolute no to offsetting

During discussions to set the EU's 2040 climate target, the spectre of international credits entering the ETS1 was raised once again. Turning the ETS1 into an offsetting mechanism would radically change its nature and mean the EU will repeat an error from its past.

During Phase 3 of ETS1 (2013–2020), over 1.6 billion international credits entered the market and wrecked the price signal, delaying emission reductions and completely undermining the effectiveness and credibility of the ETS1 for a decade. The use of carbon credits generated under the Kyoto Protocol hampered the functioning of ETS1 by inflating the oversupply of emission allowances, thereby lowering the incentive for European industry to decarbonise. In addition, confidence in the climate benefits of these cheap credits plummeted due to their lack of environmental integrity and the harm some of these projects caused to local and indigenous communities.

Recent analysis shows that there is no evidence to suggest that bringing international credits awarded under the Paris Agreement's Article 6 system into the ETS1 would lead to significantly different results.

Policymakers must not forget their (very recent) history – and avoid hurtling into this mistaken decision once again with their eyes wide open. Any integration of international credits risks diverting much-needed investments away from the EU's green industrial transformation to dubious crediting projects outside the EU.

Offsetting has absolutely no place in a credible EU ETS, not in ETS1 nor ETS2. There can be no ifs, buts or maybes: do not integrate offsets (such as international credits) into the EU ETS.

6. Keep removals out of the system

In the short term, there is a role for the ETS1 to support the development of the carbon removals (CDR) sector in the EU through the revenues it generates, but the suggestion to integrate removals directly in the ETS1 must be considered an absolute non-starter. Addressing the climate crisis requires both emission reductions (primarily) and removals (secondary), not either-or. The logic of zero-sum offsetting must be rejected.

The ETS1 must function first and foremost as an effective decarbonisation mechanism: there are still many emissions left to abate across ETS1 sectors, and mitigation deterrence is a key concern. This risk was already recognised by the co-legislators during the previous EU ETS revision – who added a guiding principle to Article 30(5)a: “ensure that [...] removals do not offset necessary emission reductions”.

Cost is a second significant challenge. Permanent removals such as Biogenic Carbon Capture and Storage (BioCCS) or Direct Air Carbon Capture and Storage (DACCS) remain far more expensive than the EUA price (BioCCS: €150–200 and DACCS: €500–1000 per tonne, vs the EUA price of €65–90 at the beginning of 2026). This trend will continue in the short to mid-term, and relying on the ETS1 to scale this sector is unrealistic. In any case, other policies and support mechanisms will be needed to mature and make this sector more viable, and are better suited to do so.

Third, the quality of the removals risks being too low to compensate for an emission under the ETS1. The Carbon Removal and Carbon Farming (CRCF) certification framework's permanent removal methodologies are fundamentally flawed. The CRCF risks mislabeling activities that increase global emissions as removals, which is an unacceptable risk for the integrity of the ETS1.

Fourth, while limits on quality and/or quantity could be set, and intermediary institutions established, any direct integration of removals would make the ETS1 an offsetting scheme again: damaging its ability to reduce emissions, potentially beyond repair.

Finally, some stakeholders (even unapologetically) want to throw carbon removals into the ETS1 as a means to drive down the carbon price. Permanent removals won't do that, but their integration would open the door to cheaper and lower-quality offsets down the road, including biochar or options that have a high risk of reversal, such as forestry and soil carbon. This may well

be the end goal of some enthusiastic CDR pushers. This risk should concern everyone who champions the ETS as an effective climate tool.

Direct integration of CDR in the ETS1 is either a dead end or the start of a slippery slope. However, there is an argument for using ETS1 revenues to invest in research and development or even to fund CDR projects. Permanent removals can be supported by options other than the carbon market, but these risk being ignored if the unconvincing and potentially destructive path of integration into the ETS1 is pursued.

7. Extend the ETS1 scope: aviation, shipping and waste

Aviation is one of the most unequal sources of climate pollution. Just 1% of people are responsible for over 50% of global aviation emissions. Yet, the ETS1 currently covers only 15% of the aviation sector's total climate impact, as it applies solely to flights between EEA airports and only to CO₂ emissions, excluding all non-carbon dioxide effects.

Extending the ETS1 to include all CO₂ emissions from flights departing EEA airports could raise an additional €9 billion annually by 2030. However, even this partial extension would remain limited in scope. It would still exclude non-CO₂ effects, which represent two-thirds of aviation's total climate effects, as well as arriving flights to the EEA. Pricing CO₂ and non-CO₂ effects of all departing and arriving EEA flights would raise an extra €96 billion annually by 2030.

Carbon leakage risks are low, and ticket demand is largely unaffected by carbon pricing. If risks are found through careful analysis, targeted measures (such as higher ETS prices on specific routes) can correct any cost-advantage of transferring through non-EEA airports.

Private jets emit 5–14 times more per passenger than commercial flights, are mostly short-haul, and their emissions output soared by 46% between 2019 and 2023. Yet two-thirds of their EU emissions fall outside ETS1 pricing due to current thresholds for aircraft weight, annual emissions, or flight numbers. Applying an ETS1 price multiplier of four (x4) to intra-EEA private jet flights could generate about €5 billion between 2025 and 2040, while a broader scheme covering all intra- and extra-EEA flights, including their non-CO₂ effects with the same multiplier, could raise up to €59 billion.

In 2024, the ETS1 generated €38.8 billion, including €2 billion from shipping. However, only 50% of emissions from extra-EEA shipping voyages are covered. Extending coverage to 100% and including smaller vessels (400–5000 gross tonnage), which emit 17.8 Mt CO₂ annually, would strengthen incentives to shift toward cleaner technologies.

The Commission should also include waste incinerators and landfills under the ETS1. Incorporating waste incineration alone would result in emission reductions of at least 4 to 7 Mt in 2030 and 18 to 32 Mt in 2040 while boosting recycling, sorting, and waste prevention. The reform should be backed by strict landfill rules, including bans already applied by some member states.

8. Remove biofuel handouts

In 2024, €100 million worth of free allowances were granted to 53 airlines to promote the uptake of biofuels in aviation. Any EU ETS funding should only be used to support technologies that can be scaled in the long-term and are truly sustainable, which is not the case with biofuels. Any free allowances should instead be limited to cleaner fuels, meaning e-fuels. If extended to shipping, such support should likewise exclude biofuels and include annual caps per technology.

Non-CO₂ effects can lead to greenhouse processes, such as condensation trails ('contrails') – the white strips often left behind by aeroplanes in the sky – which can have a climate-warming effect up to three times higher than carbon dioxide. It is important that the scope of Monitoring, Reporting, and Verification (MRV) for non-CO₂ effects is automatically extended to cover all departing and arriving flights to give fuller oversight of aviation's total climate impact.

In 2019, fewer than 5% of flights were responsible for around 80% of European contrail warming. Adjusting flight routes or altitudes to avoid contrail-forming conditions can cut non-CO₂ effects by almost two-thirds with only marginal increases in costs (0.08%) and fuel use (0.11%). To prevent over-incentivisation, contrail avoidance should be supported with a carefully limited share of free allowances, which would have otherwise been gifted to airlines for the uptake of e-kerosene.

9. Null and void the zero-rating of biomass

The burning of biomass in installations covered by the ETS1 has increased steadily in both absolute and relative terms, and in 2024, it accounted for more than a fifth of total emissions from ETS1 stationary installations. However, the Renewable Energy Directive (RED) assumes a "zero-rating" of biomass in the energy sector, so these extra emissions occur in addition to EU ETS emissions but are not priced. The justification for incentivising biomass emissions is the incorrect assumption that emissions from biomass harvested and burned are magically compensated due to the automatic and swift regrowth of the burned biomass. Yet it could take decades to centuries for the replanted trees (and the carbon sequestering ecosystem they were part of) to mature: the European Academies Science Advisory Council concludes that biomass burning is "not effective [...] and may even increase the risk of dangerous climate change."

The zero-rating creates a perverse incentive to swap fossil fuels for biomass throughout the EU ETS. Burning woody biomass for power generation actually emits more than coal in the short term, with carbon debts persisting for up to a century if the forest actually regrows (and isn't replaced by a tree plantation, agriculture or urban development).

Additionally, the RED framework is riddled with loopholes, and the criteria are simply not strong enough to ensure that any burned biomass is 'sustainable'. To make matters worse, the EU land sink is being pushed to its limits and risks crashing. Member states are not on track to reach their LULUCF targets, largely because of increased biomass burning for energy – half of all harvested woody biomass is being burned in the EU.

Disincentivising the burning of biomass in ETS1 installations (power and industry, as well as biofuels) must be a priority for this revision. In Paris Agreement relevant timeframes, the atmospheric impacts of a CO₂ molecule are the same whether originating from a tree or a barrel of oil.

10. Leave ETS2 alone in the 2026 EU ETS review

ETS2 is outside of the scope of this EU ETS review, and must be kept off the negotiating table. Despite the fact that ETS2 hasn't even started yet and is scheduled to be reviewed in 2028, it's likely that its opponents will try to (ab)use the 2026 review to weaken the system.

ETS2 has already been significantly weakened by policymakers via the one-year delay of ETS2 and the reform of MSR2. Further postponement and revision of key ETS2 elements would substantially weaken the policy's delivery of climate action and undermine the regulatory stability that businesses and households rely on to make long-term investment decisions. NGOs and progressive industry alike have called for policymakers to leave ETS2 alone and to instead focus on actions that will increase the system's social fairness and environmental effectiveness. The 2028 ETS2 review will be an important chance to strengthen the scheme.

Policy recommendations for a fair and effective ETS2

1. Do the ETS2 implementation homework

Member states are running heavily behind schedule in implementing ETS2 and need to catch up by urgently transposing it into national law and delivering strong Social Climate Plans.

A tracker, regularly updated by non-profit organisation IETA, shows that almost a third of member states still have to transpose the ETS2 part of the ETS Directive, despite the deadline of 30 June 2024. Member states that haven't transposed the directive don't get access to the Social Climate Fund or any other ETS2 revenues, thereby holding back billions of euros available for their own citizens.

Even worse, of the EU27, only one Social Climate Plan has been approved by the European Commission, and six others have been submitted for assessment. 20 member states are yet to submit their Social Climate Plans outlining how they will support vulnerable households through the energy transition.

The quality of circulated final and draft Social Climate Plans varies, as analysed in the Social Climate Fund Tracker organised by REScoop.eu and CEE Bankwatch. A strong Social Climate Plan must ensure that investments and policy actions are effectively targeting those who need it most.

Investments should make energy efficiency, renewable energy and electrified solutions more affordable for citizens, including through energy-saving renovations, decarbonisation of heating and cooling systems, zero-carbon vehicles, and participation in energy communities. As these investments can take time to put in place, they should be complemented by direct income support in the interim to provide support that protects the most vulnerable societal groups.

SCPs should be drafted – and implemented – based on a meaningful, inclusive and transparent stakeholder consultation process. Some member states (e.g., Poland) have also set up monitoring committees to oversee the Plan’s implementation – a good practice that should be emulated by all countries.

2. Transparent spending of ETS2 revenues, based on inclusive decision-making

ETS2 will generate revenues worth hundreds of billions of euros, and strategic allocation of these funds can help make the energy transition away from fossil fuels affordable for households. According to the directive, all ETS2 revenues must be spent on lowering emissions in buildings and road transport, and that priority should be given to measures addressing the social impacts of ETS2. The revenues should be invested into a mix of investments in long-term solutions, such as socially targeted support schemes for renovations, energy communities, zero emissions transport options, public transport and renewable energy infrastructure.

Transparent reporting and accountability from both member states and the Commission is critical to ensure that all ETS2 revenues are earmarked as intended, and do not become filtered into member state general budgets. The European Commission should then duly monitor the spending of earmarked revenue to ensure that member states spend funds in full on climate action, prioritising social measures, as outlined in the EU ETS directive, and take appropriate action should governments fail to uphold their commitments.

Member state governments must outline the environmental and social impacts of financed measures, and must make their plans publicly available to allow civil society to scrutinise whether or not revenues are being spent in a socially fair and environmentally effective manner. The Commission should organise civil society missions to visit different member states and hear from NGOs how ETS2 revenues are being spent.

To ensure effective spending, it is important that NGOs and other stakeholders are included in the overall planning of how ETS2 revenues will be managed. Member states have set up Multilevel Climate and Energy Dialogues through the Governance Regulation, which are suitable and existing fora that can bring together all relevant stakeholders to co-decide how ETS2 revenues are best spent – thereby cultivating social acceptance for the system. Through annual public events, member states and the Commission can exchange best practices on ongoing ETS2 and SCP implementation.

3. Expand and extend the Social Climate Fund

The Social Climate Fund represents a positive step towards tackling energy and transport poverty and supporting vulnerable households during the transition. However, the fund should be expanded and extended to enhance its impact and improve its reach. The fund is currently capped both in size and time, at €86.7 billion and ending in 2032. The fund is currently financed by €65 billion in ETS2 revenues and supplemented by an additional €21.7 billion in co-financing from member states. 25% of project financing under the Social Climate Plans must come from member states, bringing total available SCF funding to €86.7 billion. There has been no impact assessment from the Commission justifying the size or why a SCF wouldn't be needed after 2032. The SCF should continue beyond its currently envisaged end date, and the cap should be removed to ensure that the proportion of funding available to support the most vulnerable increases as the ETS2 price rises over time.

Member states should also top up financing for their Social Climate Plans by increasing their co-financing beyond the mandatory minimum of 25% co-financing rate and by borrowing from the EIB Frontloading Facility. The facility, announced in February 2026, allows member states to access additional funding – guaranteed by future ETS2 revenues – to support households ahead of the start of ETS2. Member states should also increase support to vulnerable households, making use of other funds and funding sources, such as revenues from early ETS2 auctioning, MSR2 allowances and ETS1, for example, the Modernisation Fund. Additional instruments to increase resources, such as wealth taxes, fossil fuel company levies (including on windfall profits) and the redirection of fossil fuel subsidies, should also be considered.

4. Implement strong complementary policies

To boost the effectiveness and fairness of the new carbon pricing scheme, EU member states must implement and pair ETS2 with complementary climate, social and fiscal policies, creating a coherent and proactive policy mix. Carbon pricing alone cannot deliver the rapid emissions reductions required in the buildings and road transport sectors. Additional climate and social policy is critical to overcome structural barriers for decarbonisation, such as limited investment capacity among vulnerable households and to ensure the energy transition is just.

Implementation of strong complementary sectoral climate policies will deliver a double benefit – emissions reductions and a lower ETS2 price for everyone, as the demand for emission allowances decreases. By implementing socially targeted climate investments and complementary policies, national governments have it within their power to make the carbon price picture less daunting for citizens and to lessen the risk of spiralling prices. Unfortunately, many governments are going in the opposite direction, as can be noticed in efforts to weaken key complementary policies such as clean heating standards or the proposed ban on new sales of CO₂-emitting vehicles. Such decisions drive the carbon price up rather than down.

Existing complementary climate policies that tackle road transport and building emissions must be fully implemented and strengthened, such as the CO₂ standard for cars and vans, the Energy

Performance of Buildings Directive (EPBD), the Renewable Energy Directive (RED), and the Energy Efficiency Directive (EED). Complementary policies that deliver emissions reductions quickly and provide a strong investment signal are particularly important. These policies include phasing out Internal Combustion Engine (ICE) vehicles and fossil fuel boilers, as well as enhanced rollout of support schemes for renovations, renewable energy communities, heat pumps, electric vehicles, charging stations, energy storage and other energy infrastructure, for example, greening corporate fleets.

Equally important are measures that limit overall road traffic, such as halting new road construction, promoting modal shifts to zero-emission public transport, encouraging active mobility (walking, cycling), and improving rail infrastructure. Countries with high income levels and that are responsible for higher shares of emissions have a greater responsibility in implementing these measures, as they contribute an outsized influence on the ETS2 price.

Further examples of social climate policy instruments that can accompany ETS2 include laws that regulate the sharing of carbon-pricing costs between tenants and landlords based on energy performance, or that modulate rent increases as a function of energy performance. Such measures do not even require any fiscal expenses.

5. Reform the energy taxation systems

Remove all fossil fuel subsidies and lower taxation on electricity to drive the demand for renewable solutions that support, rather than distort, the ETS2 price signal. Eurostat data shows that, on average across the EU, households pay more than twice as much for electricity as for fossil gas. This distortion largely stems from levies to fund the energy transition being loaded into electricity bills, while fossil gas production remains lightly taxed. Electricity prices are also inflated by Europe's continued dependence on fossil fuels, which exposes consumers to volatile global fuel markets. On top of this, EU fossil fuels are heavily subsidised; in 2023, subsidies reached €111 billion, with almost half of them having no planned end date.

The imbalance in energy taxation discourages the shift to electric systems, undermining decarbonisation efforts. Member states can reinforce the ETS2 price signal and make it less regressive by removing harmful subsidies, taxing fossil fuel companies (including on windfall profits), applying progressive levies on high-emission sectors, and ensuring fair contributions from the wealthiest people and companies.

Regarding sectors covered by ETS1, in addition to receiving carbon pricing exemptions, aviation escapes €21.3 billion and shipping €24 billion in taxes each year. These tax exemptions directly contradict the EU's climate commitments and the polluter pays principle. It is unjustifiable that airlines pay no kerosene tax and no VAT on international tickets, while rail operators face energy taxes, VAT, and high track access charges in many countries. Gaps left by the Energy Taxation Directive make it even more urgent that ETS1 is extended at least to all departing flights from the European Economic Area (EEA) and private jet flights, as well as 100% of extra-EEA shipping voyages and smaller vessels (400–5000 gross tonnage).

Narrative and messages

Although the EU Emissions Trading System is packed with technical detail and heaps of jargon, it is possible to cut the communications monster down to size by using key messages and narratives which help detangle what the EU ETS is really about at its core.

Through effective storytelling, direct communication, and simple messaging, it is possible to explain not only how the carbon pricing scheme connects to people's lives but also why policymakers need to defend and continue to improve the ETS. During the LIFE ETX project, we showed through the 'Human Stories' series how the EU ETS can be a force for good: decarbonising Europe and benefiting people's lives.

Here's how to approach the ETS monster:

Key messages

Climate

- Carbon pricing works: While EU ETS is imperfect, ETS1 has helped halve emissions from heavy industry and power over the past 20 years.
- Polluters must pay: If you break it, you fix it. And if you continue to break it, you should compensate for the damage you cause, and fund solutions.

Social justice

- Leave nobody behind: The energy transition involves everyone, and people most in need of support should be empowered to play their part.
- Ensure fairness: Wealthy and highly polluting citizens should pay more for their emissions whereas vulnerable households must be well supported in the climate and energy transition.

Governance

- Part of the plan: The EU ETS is a critical element in the EU's approach to reach its 2050 climate target, and a key source of financing for social climate policies that support an inclusive transition. But it can't do it alone, complementary policies must be part of the policy mix.
- Spend wisely: The EU ETS provides hundreds of billions to fund climate action in member states. These funds must benefit people and contribute to the safety of our planet. Any EU ETS support to technologies must be limited to truly sustainable and scalable solutions in the long term.
- Ensure transparent and inclusive decisions: Spending of revenues must follow principles of transparency and accountability. Civil society should be involved in deciding where funds are allocated.

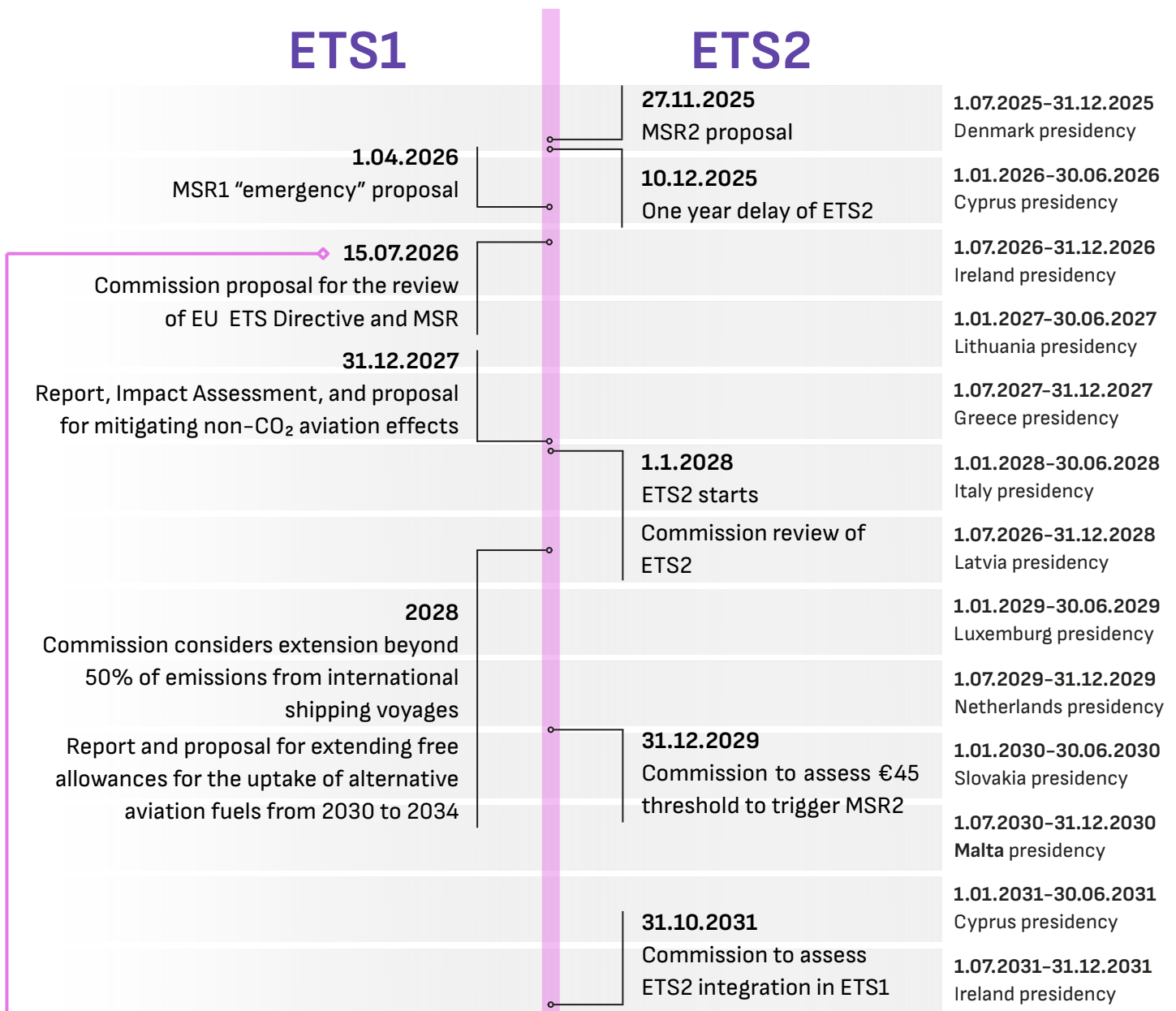
Key narratives

- **Urgency:** The societal cost of climate inaction is huge, and the speed of emissions reductions must increase rapidly.
- **Energy security:** In an increasingly tense geopolitical context, reducing dependence on volatile imported fossil fuels is both an economic and strategic imperative.
- **Good for people:** Effective implementation of the EU ETS improves health by reducing air pollution and limiting the impact of climate breakdown on society.
- **Good for clean business:** The EU ETS increases pressure to create a clean and secure European energy system based on renewables and creates opportunities for European industry, including key green technologies such as heat pumps, electric vehicles, energy storage, wind, and solar.
- **Driving global climate ambition:** By pricing domestic and imported CO₂, the EU ETS, combined with the Carbon Border Adjustment Mechanism, is an example of an effective regional climate policy that drives ambition worldwide.
- **Cost of living:** The real threat to affordability isn't a carbon price but continued dependence on polluting and price-volatile fossil fuels. The roll-out of renewables will help bring energy prices down and make them more stable, and ensure investments and money stay in the EU.

Connecting

- **Keep it simple:** Do not communicate all the jargon and technicalities; approach the issue in a simple, storytelling manner.
- **Make it relatable:** Connect the issues to people's lives. Reducing emissions is not about reaching some political target but about improving health, quality of life and security.
- **Go direct:** The planet is warming at an alarming rate, and it is crucial to remind policymakers that this is not tomorrow's problem.

Advocacy moments/timeline



Key moments following the EU ETS proposal:

- Deadline for amendments in the ENVI
- Vote in the ENVI committee
- Vote in the European Parliament
- Environmental Council position
- Trilogues
- Publication in Official Journal & entry into effect

Key policymakers

European Commission

Aspects related to ETS1, ETS2 and the Social Climate Fund are covered in the portfolio of several Commissioners and Directorate-Generals. Commission President Ursula von der Leyen assigned Wopke Hoekstra as the Commissioner for Climate, Net-Zero and Clean Growth, who is responsible for the EU ETS. The EU ETS lead in the Hoekstra cabinet is Olivia Gippner. Hoekstra reports to Commission Vice President Teresa Ribera, who is responsible for the portfolio 'A Clean, Just and Competitive Transition'.

The EU Emissions Trading System is a climate policy tool, and the Directorate-General for Climate Action (DG CLIMA) in the European Commission is responsible for overseeing the implementation of this Directive and draft proposals for legislative change. DG CLIMA leads the European Commission's efforts to fight climate change at EU and international level. Head of DG CLIMA is Kurt Vandenberghe. He sets the direction and oversees the work of the Directorate-General, following the political guidelines set by Commissioner Hoekstra. Within the DG, Carbon Markets and Clean Mobility (CLIMA.B), leads the development and implementation of the EU ETS, which is currently led by Beatriz Yordi. She oversees the directorate's work on the EU ETS Directive and coordinates the different departments. Unit B.1 led by Mette Quinn, leads on the EU ETS review and unit B.5 led by Marcos Gonzales Alvarez, leads on the Social Climate Fund and ETS2 implementation.

Certain elements of the EU ETS and the Social Climate Fund, as well as highly related policies, are in the portfolios of additional Commissioners and Directorate-Generals. These include Stéphane Séjourné, Executive Vice-President for Prosperity and Industrial Strategy (DG GROW), Dan Jørgensen, Commissioner for Energy and Housing (DG ENER), Roxana Mînzatu, Executive Vice-President for Social Rights and Skills, Quality Jobs and Preparedness (DG EMPL) and Apostolos Tzitzikostas, Commissioner for Sustainable Transport and Tourism (DG MOVE).

The Environment Council (member states)

The EU Emissions Trading System is a Directive that falls within the remit of the EU environment ministries. It is thus discussed and agreed in the Environment Council.

For the ETS reform to be adopted a qualified majority in the Environment Council is required. It is therefore very important to understand the positions of the EU 27 member states on key aspects of the ETS Directive, and advocacy targeted towards environment ministers will be critical throughout the legislative process. It is also important to liaise with permanent representations in Brussels and to keep track of upcoming Council meetings.

European Parliament

The Committee responsible for revising the EU Emissions Trading System in the European Parliament is the Environment, Public Health and Food Safety (ENVI) Committee. In this Committee, one rapporteur will be appointed, responsible for drafting the Committee's report on the European Commission's proposal. The rapporteur will lead Parliament's political process towards its final, consolidated version. The parliamentary groups nominate a shadow rapporteur who will support the lead rapporteur in the drafting of the report at the committee stage. The committee's report will first be voted on in ENVI and thereafter in plenary. It must be approved by a simple majority to become the official position of the Parliament ahead of trilogue negotiations with the Commission and Council. During the EU ETS revision process, the ENVI Committee will receive input and may share competences on relevant and specific issues with other parliamentary committees, namely the Industry, Research and Energy Committee (ITRE), the Budgets Committee (BUDG) and the Transport and Tourism Committee (TRAN).

Key readings and resources

Readings

ETS1

Don't mess with the ETS (CMW priorities for the 2026 EU ETS review)

<https://carbonmarketwatch.org/publications/dont-mess-with-the-ets/>

CAN Europe position on the EU Emissions Trading System (ETS)

<https://caneurope.org/publications/can-europe-position-on-ets/>

EU ETS 101 introductory guide

https://carbonmarketwatch.org/wp-content/uploads/2024/02/CMW_EU_ETS_101_guide_2024_v04-1.pdf

Trends in the Emissions Trading System in the European Union, 2005-2024

<https://life-effect.org/project/trends-in-the-emissions-trading-system-in-the-european-union-2005-2024/>

Five reasons why attacking the EU carbon market is economic self-sabotage

<https://www.bruegel.org/first-glance/five-reasons-why-attacking-eu-carbon-market-economic-self-sabotage>

EU Industry Associations Increasingly Misaligned with Corporate Support for the Emissions Trading System - A Summary of Corporate and Industry Advocacy on the EU ETS

<https://influencemap.org/insight/EU-Industry-Associations-Increasingly-Misaligned-with-Corporate-Support-for-the-Emissions-Trading-System-37860>

Facts over Fiction: Why the EU ETS is key for a competitive, secure Europe

<https://www.e3g.org/publications/facts-over-fiction-why-the-eu-ets-is-key-for-a-competitive-secure-europe/>

The Emissions Aristocracy

<https://carbonmarketwatch.org/publications/the-emissions-aristocracy/>

European Commission's 2025 Carbon Market Report

https://climate.ec.europa.eu/news-other-reads/news/2025-carbon-market-report-eu-ets-lowers-power-sector-emissions-and-expands-maritime-transport-2025-12-03_en

Resource library LIFE ETX Project (2021-2024)

<https://etxtra.org/resources/>

ETS2

CAN Europe position on ETS2

<https://old.caneurope.org/content/uploads/2025/08/Position-paper-ETS2-CAN-Europe-August-2024.pdf>

ETS2 101 introductory guide

<https://life-effect.org/training-modules/>

FAQ: Social Climate Fund

<https://life-effect.org/project/faq-social-climate-fund/>

Green Solidarity: Guiding Principles for a Truly Just Social Climate Fund

<https://life-effect.org/project/green-solidarity-guiding-principles-for-a-truly-just-social-climate-fund/>

Race to the top: Reform and investment proposals for the Social Climate Plans

<https://bankwatch.org/publication/race-to-the-top-reform-and-investment-proposals-for-the-social-climate-plans>

Safeguarding social justice in EU climate finance: Unpacking the MFF-SCF link

<https://life-effect.org/project/safeguarding-social-justice-in-eu-climate-finance-unpacking-the-mff-scf-link/>

Why the MSR2 non-paper should be a non-starter

<https://life-effect.org/project/why-the-msr2-non-paper-should-be-a-non-starter/>

Find further readings, including country-specific insights on the LIFE Effect website:

<https://life-effect.org/publications/>

Resources

Climact's ETS Simulator

<https://my.climact.com/tools/ets-simulator>

ETX Module: EU ETS data and legislative sources

<https://etxtra.org/etx-module-eu-ets-data-and-legislative-sources/>

Social Climate Fund Tracker

<https://www.rescoop.eu/policy/financing-tracker/social-climate-fund>

IETA's ETS2 National Transposition Tracker

<https://www.ieta.org/ets2-tracker>

ETS2 101 Training Modules

<https://life-effect.org/training-modules/>



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