

Improving EU ETS benchmarks

Response to the European Commission's public consultation on EU ETS benchmarks

Sandbag welcomes the opportunity to contribute to the public consultation on the European Commission's proposed revision of the benchmark values of free allocation of emission allowances (2026-2030).

Windfall profits for steel but not for recycling

We note that the ETS Directive, through Article 10a(2)(e), has granted a freeze to the **hot metal** benchmark, rewarding primary ironmaking and extended this benchmark to the production of direct reduced iron (DRI), which has much lower emissions (0.39 tCO₂/t in the EU, according to the JRC¹, compared to 1.248 EUA for the benchmark) creating **windfall profit** of 0.858 EUA per tonne of DRI produced.

The proposed **EAF carbon steel** and **EAF high alloy steel** benchmarks will lead to a nearly three-fold increase in free allocation to electric arc furnaces compared to the 2021-25 period. This is because in 2021-25, the value of these benchmarks included indirect emissions, even though the actual allocation was only based on direct emissions. This exception concerned 14 benchmarks under the regime of "exchangeability of fuel". Now that this regime was abolished in 2024, free allocation is directly linked to the benchmarks. However, the values of the benchmarks were still calculated based on both direct and indirect emissions, resulting in a big increase in free allocation, creating more **windfall profits**.

	Emissions (incl indirect) 2016-17	Emission intensity (weighted avg, incl indirect)	Preliminary free allocation 2021	Free allocation (weighted avg) per tonne 2021	Benchmarks (= free allocation per tonne) 2026-30
EAF carbon steel	9,959,740	0.255	2,050,637	0.052	0.142
EAF high alloy steel	8,687,004	0.325	2,185,759	0.082	0.176

We regret that the benchmarks are still **very dependent on processes** rather than products, despite the requirement set in Article 10a(1) to reform them so that they "should be independent of the feedstock and the type of production process". As a result, steelmaking receives most of its allowances based on the amount of primary ore transformed whereas the use of alternative feedstock such as recycled metal is not rewarded.

We believe that there is no reason for the 14 benchmarks under the former regime of exchangeability of fuel differently to be calculated based on both direct and indirect emissions, and that they **should be based on the direct emissions only** of the 10% installations with lowest direct emissions. The new value of those benchmarks should also be calculated by applying a reduction rate from an initial value that only covers direct emissions.

¹ JRC (2023), *Greenhouse gas intensities of the steel, fertilisers, aluminium and cement industries in the EU and its main trading partners*

Turn fallback sub-benchmarks into product benchmarks

The heat and fuel benchmarks (together called “fallback”) were calculated based on the assumption that biomass is emissions-free, which is why the 10% installations with the lowest emissions have driven down these benchmarks to low values. This should be changed: biomass is not zero-emission and its use is unsustainable on a large scale. Thus, emissions from biomass use should be accounted for in ETS yearly reporting.

However, we don't think the fallback benchmarks should simply be adjusted upwards as a result. Instead, the opportunity should be seized to **create new product benchmarks that are independent of production processes**, as commanded by Article 10a(1). In this sense, we welcome the Commission's initiative to cover some of the installation currently using fallback benchmarks under a new set of benchmarks.

However, the proposed benchmarks and their calculation method are both disappointing. To be independent of production processes, **they should be set per volume of goods produced** (e.g. per tonne of sugar, refractory ceramics etc.). Instead, the Commission proposes **fallback sub-benchmarks** which will keep awarding free allocation based on the amount of energy (heat or fuel) consumed, encouraging waste and discouraging efficiency, circularity and alternative processes.

It is possible to replace fallback sub-benchmarks with actual **product benchmarks**. All this would require is to collect 2021-22 production data for the products considered and calculate benchmark values based on the **10% lowest emission plants producing those goods over 2021-22**. To avoid litigation risk on grounds of preferential treatment, a reduction rate could be applied equal to 6 times the average annual reduction rate of all benchmarks, due to the 6 years between 2022 (date of the collected data) and 28 (middle of the 2026-30 period), like for (most) other benchmarks.

Although this method would differ from using a 2007-8 base year with floored and capped reduction rates, **the methodological difference would be very minor**: it would give the same results if the 10% lowest emission plants have reduced their emission intensity by amounts withing the current cap and floor (0.3%-2.5% annually) since 2007, i.e. more than 6% or less than 50%, which is the case for most other products.

Methodological differences between benchmarks are **not a new idea**. The regime of exchangeability of fuel is an example of differentiated methodologies across benchmarks, and there are many more, such as the process emissions benchmark which follows yet another very different one. And the Commission's own proposal to create fallback sub-benchmarks covering only part of the installations currently covered by the fallback benchmarks would also **create a separate regime**.

So we do not see a greater risk of challenge in applying product benchmarks instead of fallback sub-benchmarks. Rather than creating windfall profits, we should seize this opportunity to – at last – create incentives for sustainable practices as required by the ETS Directive.