# EU ETS review: what matters

**Arbeitsgruppe Emissionshandel, 4 November 2026**

Adrien Assous, Sandbag

# Legislative context

**Market Stability Reserve: invalidation**

- Threshold increased to 700m
- Possible x% annual decrease

**EU ETS Directive & MSR**

- COM proposal 17 July
- Draft ENVI proposal 11 September
- Amendments filed 6 Oct
- Vote in ENVI 1 December
- Vote in Plenary 14-17 December
- Trilogue

sandbag
smarter climate policy

# Commission vs. ENVI

| | Current | Commission | EP ENVI |
|---|---|---|---|
| LRF | 4.4% | 3.7%, then 1.7% | 3.4%, then 2.3% |
| International credits | no | Included in cap | Included in cap |
| Removals | no | +250m allowances | +250m allowances |
| MSR thresholds | 400-833 (but 180m not counted) | 400-833 (full amount) -4% annual decrease | ? |
| MSR invalidation | 700m – x% | 700m – x% | 700m – x% |
| MSR release rate | 100m | Reduced | ? |
| NER | 200m transfer to MSR | 400m to IDB/IB | 400m to IDB/IB |
| Free allocation | Up to 46% | Up to 47% | Up to 47% |
| Benchmarks red. rate | Min -2.5% | Min -2% | Min -2% |
| CBAM factor | 0% in 2034 | 0% in 2038 | 0% in 2038 or 2034 |
| Extra EU flights | no | Departing <5000km | Departing <5000km |
| Shipping ext, waste | no | yes | yes |

# Emissions scenarios

## 2024 impact assessment for EU Climate Law

| | EU-wide reduction | EU ETS reduction | EU ETS reduction with extensions |
|---|---|---|---|
| S1 | 75% from 1990 | 80% from 2005 | 79% from 2005 |
| S2 | 85% from 1990 | 88% from 2005 | 87% from 2005 |
| S3 | 95% from 1990 | 92% from 2005 | 91% from 2005 |

## Key metric to assess scenario likelihood: surplus / annual emissions

Surplus = EUA in circulation + reserves

## In 2026: 2,190 / 1,139 = 1.7x

# Simulation results

(based on Sandbag's EU ETS Simulator)

# Commission's proposal

With invalidation threshold of 700m

| Proposal | Cap 2040 (vs. 2005) | Emissions (m tCo2) | In circulation + NER | MSR | Surplus / emissions 2040 |
|---|---|---|---|---|---|
| Current | -99% | 177 (**S3** – 95%) | 80 | 600 | 3.8 x |
| Current | -99% | 274 (**S2** – 85%) | -294 | 200 | -0.3 x |
| + MSR thresholds + TNAC | -99% | 274 (S2 – 85%) | -281 | 430 | 0.5 x |
| + End of NER transfer to MSR | -99% | 274 (S2 – 85%) | -81 | 230 | 0.5 x |
| + Extensions | -99% | 301 (S2 – 85%) | -100 | 230 | 0.4 x |

# LRF

## Scenario S2 (85% EU-wide domestic reduction)

| LRF 2031-35; 2036-40 | Cap 2040 (vs. 2005) | In circulation + NER | MSR | Surplus / emissions 2040 |
|---|---|---|---|---|
| Current: 4.4% - 4.4% | -99% | -100 | 230 | 0.4 x |
| COM: 3.7% - 1.7% (w/o removals) | -86% | 648 | 854 | 5.0 x |
| ENVI: 3.4% - 2.3% (w/o removals) | -88% | 800 | 751 | 5.2 x |
| 4.4% - 1.7% (w/o removals) | -89% | 498 | 419 | 3.1 x |
| 4.4% - 2.7% (w/o removals) | -94% | 364 | 230 | 2.0 x |
| 4.4% - 2.7% (w/o removals, limit aviation access) | -97% | 421 | 296 | 2.6 x |

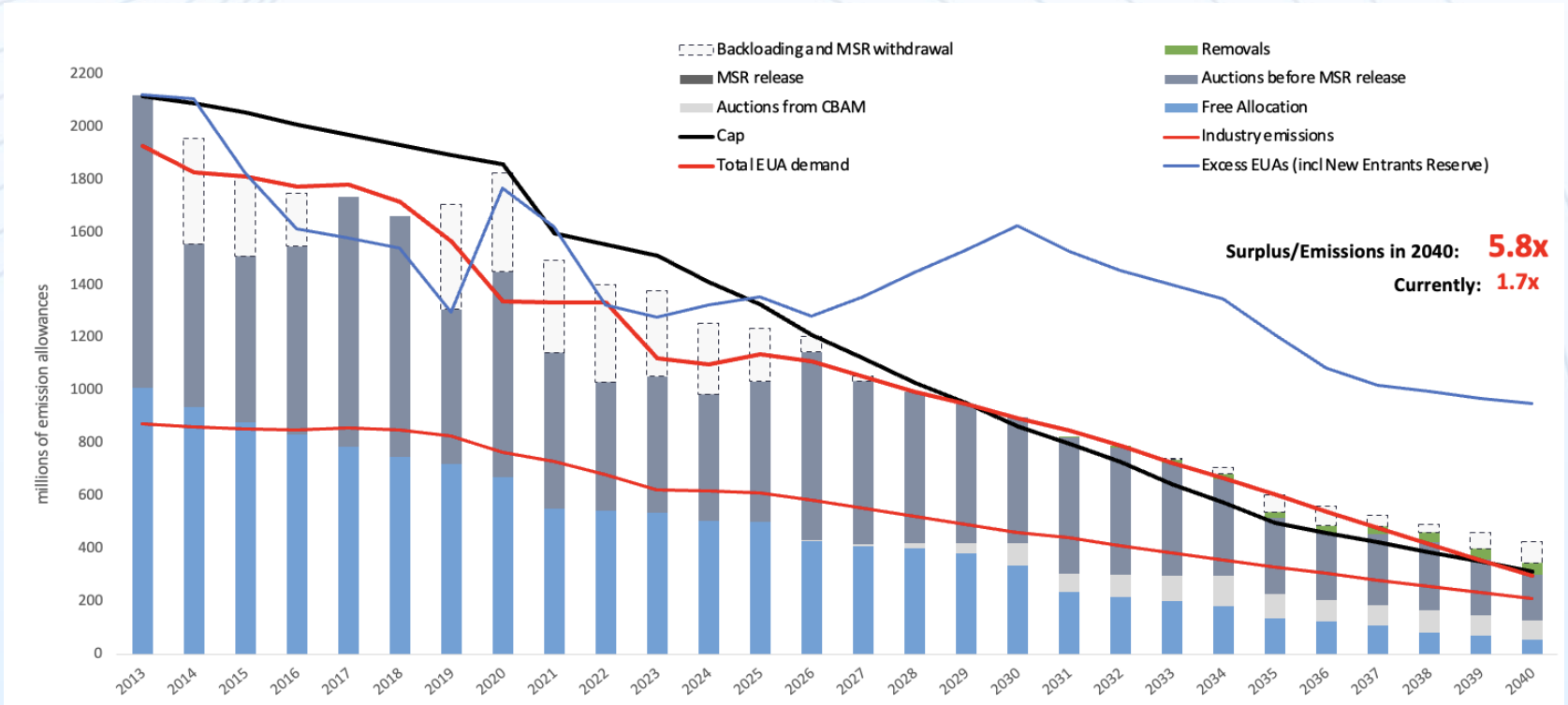
# Removals: +250m EUA

## Based on COM

- Surplus 2040:
  - 1,733m EUA

## COM vs. ENVI

- COM: up to 1.04 EUA per CDR
  - CDR supply conditional
- ENVI: no price limit
  - CDR unconditional



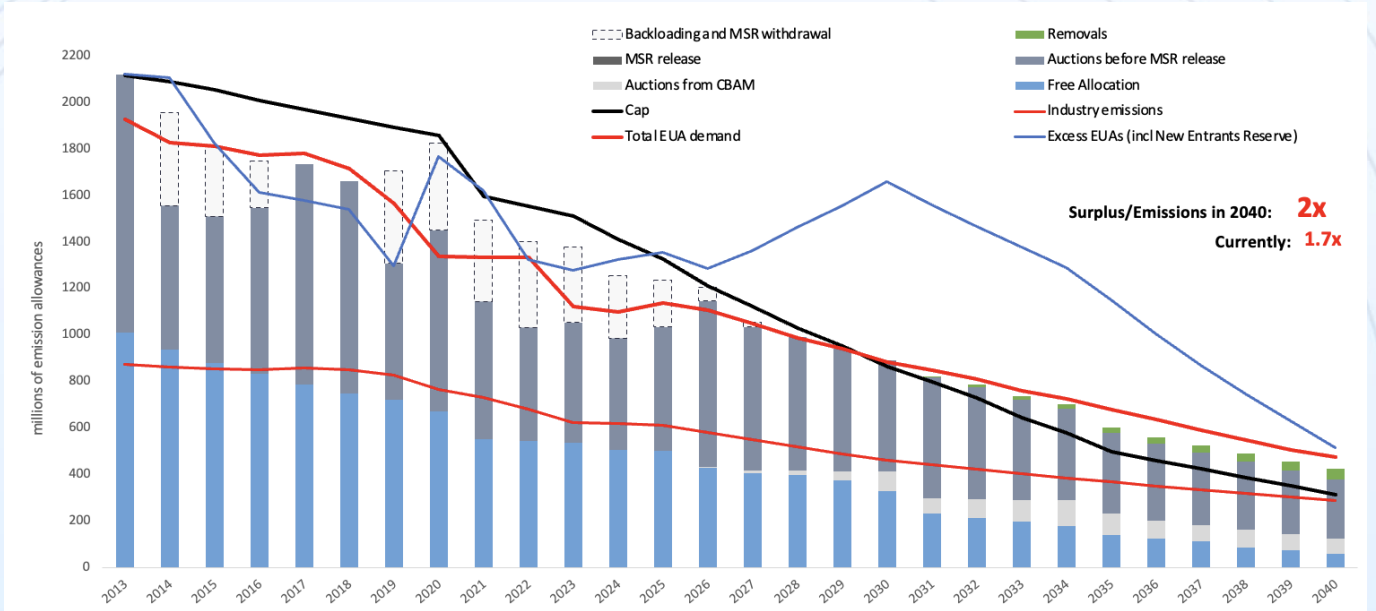

| | 2031 | 2032 | 2033 | 2034 | 2035 | 2036 | 2037 | 2038 | 2039 | 2040 |
|---|---|---|---|---|---|---|---|---|---|---|
| CSCF | 1.00 | 1.00 | 1.00 | 1.00 | 0.79 | 0.81 | 0.75 | 0.68 | 0.62 | 0.55 |
| Surplus / Em | 2.3x | 2.4x | 2.5x | 2.7x | 2.9x | 3.1x | 3.4x | 4x | 4.7x | 5.8x |

| In 2040 | | | |
|---|---|---|---|
| Cap | Emissions | MSR | Excess EUA |
| -86% | -87% | 780m | 953m |

# S1 scenario (-75% reduction)

Based on COM, with removals

- Surplus 2040:
  - 936m EUA = 2.0x
  - Emissions = 477mt




| | 2031 | 2032 | 2033 | 2034 | 2035 | 2036 | 2037 | 2038 | 2039 | 2040 |
|---|---|---|---|---|---|---|---|---|---|---|
| CSCF | 1.00 | 1.00 | 1.00 | 1.00 | 0.81 | 0.83 | 0.76 | 0.69 | 0.63 | 0.56 |
| Surplus / Em | 2.3x | 2.3x | 2.4x | 2.4x | 2.3x | 2.2x | 2.2x | 2.1x | 2.1x | 2x |

| In 2040 | | | |
|---|---|---|---|
| Cap | Emissions | MSR | Excess EUA |
| -86% | -79% | 419m | 517m |

# 4% annual decline of the invalidation threshold

sandbag
smarter climate policy

Based on COM with removals

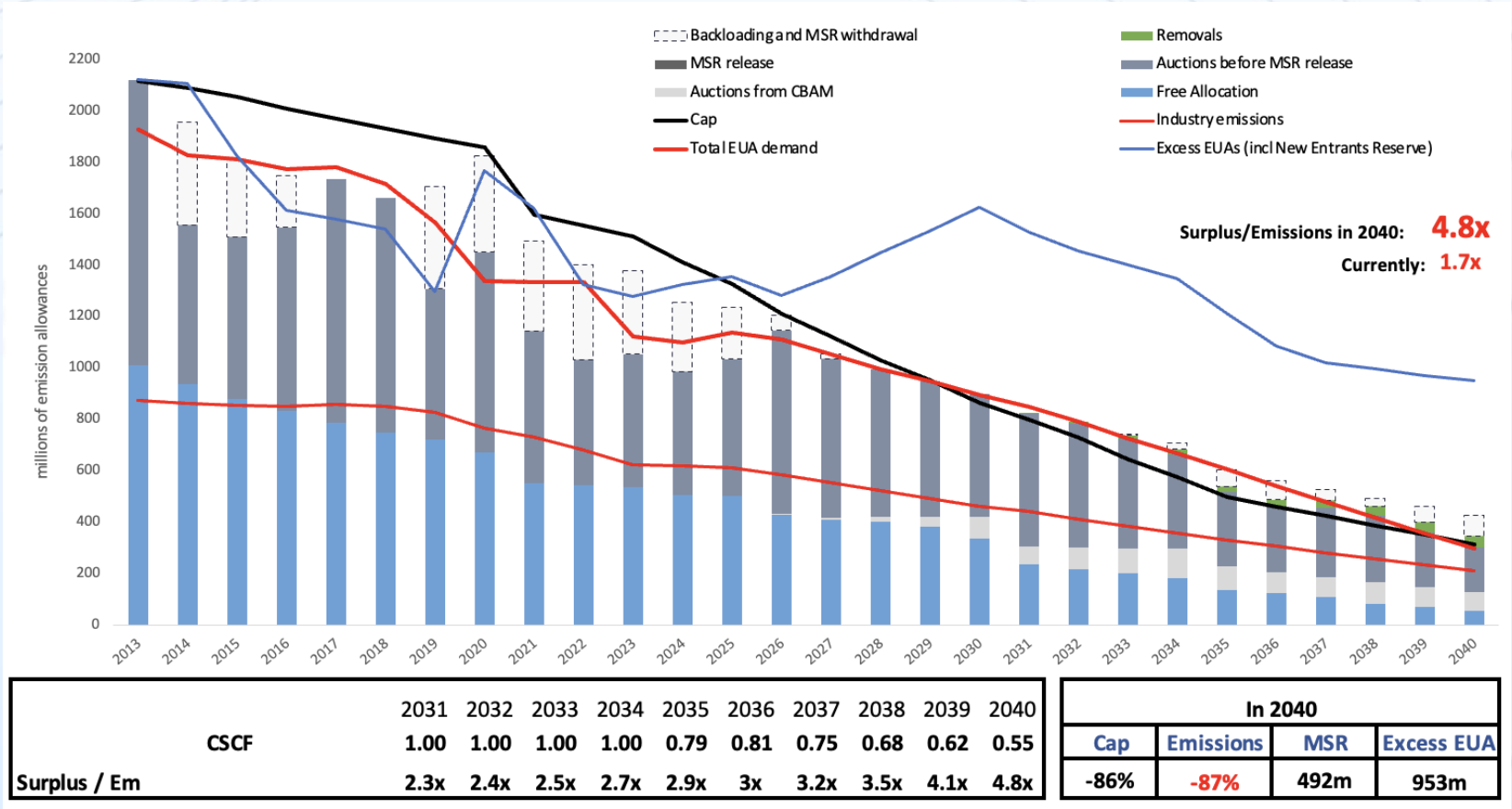
- Surplus 2040:
  - 1,445m EUA

No decline
5.8 x



4% annual decline
4.8 x

LRF is equivalent to 9-16%




| | 2031 | 2032 | 2033 | 2034 | 2035 | 2036 | 2037 | 2038 | 2039 | 2040 |
|---|---|---|---|---|---|---|---|---|---|---|
| CSCF | 1.00 | 1.00 | 1.00 | 1.00 | 0.79 | 0.81 | 0.75 | 0.68 | 0.62 | 0.55 |
| Surplus / Em | 2.3x | 2.4x | 2.5x | 2.7x | 2.9x | 3x | 3.2x | 3.5x | 4.1x | 4.8x |

| In 2040 | | | |
|---|---|---|---|
| Cap | Emissions | MSR | Excess EUA |
| -86% | -87% | 492m | 953m |

sandbag
smarter climate policy

# Alternative proposals…

## (more details here)

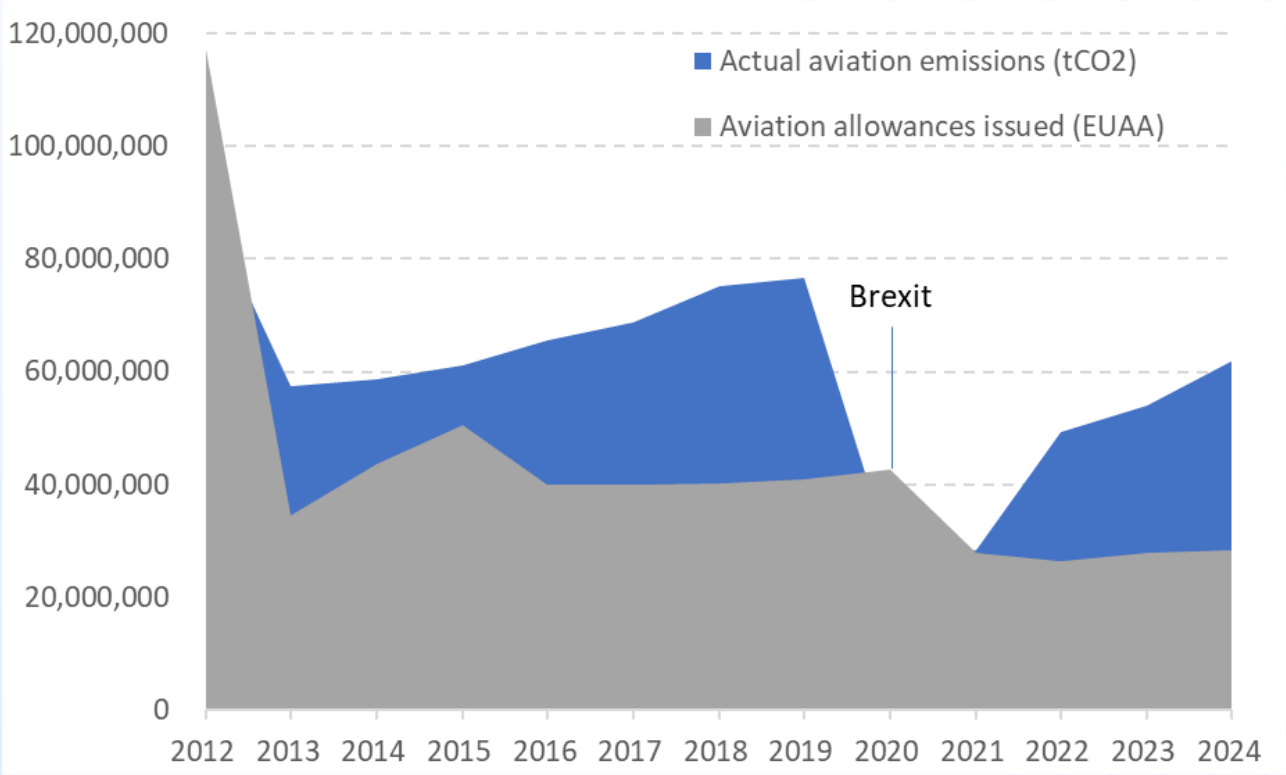
# Aviation: put a seatbelt on allowances

## Flying economy

- Cap exceeded consistently
- Buying general allowances is cheaper than abatement
- Removals are uneconomical
- Demand uncertainty affects other sectors

Demand from intra-EU flights (source: Sandbag)

| 2040 emissions scenario | 2040 EU ETS emissions (mt CO2) | 2040 aviation emissions (mt CO2) | Aviation net demand 2031-2040 (mEUA) |
|---|---|---|---|
| IA S3 (-95%) | 177 | 28 | 261 |
| IA S2 (-85%) | 274 | 29 | 268 |
| IA S1 (-75%) | 443 | 31 | 283 |
| 2040 = 2024 | N/A | 62 | 503 |



# Aviation: put a seatbelt on allowances

**Limit the surrending of general allowances**

- Re-introduce aviation allowances (EUAA)
- Airlines can surrender EUAA + a proportion of EUAs, decreasing from [100%] to [0%]
- This would raise air fares, revenues from EUAA sales, enable switch to rail, removals, efuels
- It would redirect funds from buying imported fuel to investing in domestic rail infrastructure, like China did
- It would allow to meet a larger share of the 90% target domestically, buying fewer imported credits

# Free allocation

**Currently**

- 54 product benchmarks, 2 fallback, 1 process emissions
  - Flat steel products are compensated per tonne of primary iron used
  - Fallback: per MWh used
  - Petrochemicals: per steam cracking operation used
  - Cement: per tonne of clinker/binder
  - …

**More desirable:**

- Benchmarks closer to finished goods
- Incentivising more efficient processes and circular practices
- More in line with CBAM

# Cross-sectoral correction factor

**Currently (based on COM)**

- Applied uniformly across all sectors
  - CBAM sectors protected by CBAM
  - Non-CBAM sectors unprotected

| | 2031 | 2032 | 2033 | 2034 | 2035 | 2036 | 2037 | 2038 | 2039 | 2040 |
|---|---|---|---|---|---|---|---|---|---|---|
| **CSCF** | **1.00** | **1.00** | **1.00** | **1.00** | **0.79** | **0.81** | **0.75** | **0.68** | **0.62** | **0.55** |

**Suggestion:**

- Apply CSCF to CBAM sectors first
- Non-CBAM sectors more likely to keep CSCF = 1

| | 2031 | 2032 | 2033 | 2034 | 2035 | 2036 | 2037 | 2038 | 2039 | 2040 |
|---|---|---|---|---|---|---|---|---|---|---|
| **CSCF** | **1.00** | **1.00** | **1.00** | **1.00** | **1.00** | **1.00** | **1.00** | **1.00** | **1.00** | **1.00** |

# Indirect cost compensation

**Currently, ICC:**

- Does not reward the use of renewable electricity
- Is based on the assumption that market power prices are always set by fossil-based generation
- Is expensive for Member States
- Will cost more with electrification and hydrogen use
- Is incompatible with the CBAM

**Proposal:**

- Make ICC dependent on the share of renewable power
  - This would compensate for the costs of adjusting to intermittent supply, dissociate ICC from CBAM scope
- Limit ICC to periods when fossil sets the marginal price
  - This would avoid over-compensation, decrease as the grid gets decarbonised

# Removals

**Keep as safety net**

- COM: purchase at price of 1.04 EUA
  - Supply kicks in when EUA prices are high enough
- ENVI: purchase at all cost, add biochar
  - Supply is unconditional, permanence issue

# List of possible improvements

| Article | Subject | Improvement |
|---|---|---|
| 9 | LRF | Increase, to avoid surplus/emission ratio increase |
| 9b | International credits | Turn into “safety net” with Art 29a |
| 9c | Removals | Avoid “purchase at any cost” approach |
| 29a | Price volatility | Use international credits; make symmetrical |
| 10a(7) | New Entrants Reserve | Leave in 200m transfer provision |
| 10a(5) | CSCF | Apply to CBAM sectors first |
| 10a(1)8, 10a(2)f | Free allocation | Reform to better match end products |
| 12(3) | Aviation | Limit access to general EUAs |
| 10a(6) | Compens. for ind costs | Incentivise non-fossil power, avoid over-compensation |
| 21(2), 10a(6) | Transparency | Avoid regression |
| MSR – Art 1(5), 1(6) | Upper threshold | Lower to compensate effect of TNAC change |
| MSR – Art 1(5a) | Invalidation threshold | Linear decline |

sandbag
smarter climate policy

# Q&A