EU Emissions Trading System and market stability reserve: competitiveness and cost-effective decarbonisation

2026/0212(COD) - 17/07/2026 - Legislative proposal

PURPOSE: to ensure that EU ETS contributes cost-effectively to the EU 2040 climate target.

PROPOSED ACT: Regulation of the European Parliament and of the Council.

ROLE OF THE EUROPEAN PARLIAMENT: the European Parliament decides in accordance with the ordinary legislative procedure and on an equal footing with the Council.

BACKGROUND: the EU emissions trading system (EU ETS) is the cornerstone of the EU’s climate policy, driving decarbonisation, competitiveness and resilience. Directive 2003/87/EC (ETS Directive) lays down the rules for greenhouse gas (GHG) emission allowance trading within the EU. The market stability reserve (MSR) for the EU ETS was established by Decision (EU) 2015/1814 (MSR Decision) to make the EU ETS more resilient in relation to supply-demand imbalances.

The proposal builds on over 20 years of experience with the EU Emissions Trading System (EU ETS), including the 2023 ETS revision. It forms the first part of a legislative package implementing the EU's legally binding 2040 climate target and aligns with the Competitiveness Compass, the Clean Industrial Deal and AccelerateEU. The proposal aims to ensure that the EU ETS continues to deliver cost-effective emissions reductions, supports the transition to climate neutrality by 2050, contributes to the 2040 climate target, and maintains the competitiveness of the EU economy. To achieve these objectives, it amends Directive 2003/87/EC and Decision (EU) 2015/1814.

CONTENT: the objective of this proposal is to ensure that the EU ETS continues to contribute in the most economically efficient and secure manner to the overall goal of reaching economy-wide carbon neutrality by 2050 and to the 2040 target, taking into account the broader policy framework and the need for all sectors to contribute to the EU climate efforts, while preserving competitiveness.

The current ETS legislation was revised in 2023 to deliver a 62% reduction in EU ETS emissions by 2030 compared to 2005. Since that revision, the EU has adopted a legally binding target of 90% reduction in net GHG emissions for 2040 compared to 1990 in order to stay on course for reaching climate neutrality by 2050.

The present proposal establishes the contribution of EU ETS to the post-2030 framework. It encompasses, *inter alia*, the following measures:

- aligns the system with the Union’s 2040 emission reduction target of **-90%**, adjusting the EU ETS reduction trajectory from 2031. This change permits the continued issuance of allowances into the 2040s;

- takes into account the possible purchase of **260 million international credits** to complement domestic action and reducing it to -85% compared to 1990, translating into additional domestic emission space in the ETS;

- integrates **domestic permanent carbon removals** into the EU ETS through the increase of cap by an amount of allowances equivalent to the quantity of removals that will be bought by the Commission, thus creating guaranteed additional emission space for the hardest-to-abate sectors and supporting the scale-up of the carbon removals industry, while ensuring control of the quality and quantity of the removals;

- reforms the market stability reserve to ensure a stable and liquid market and smooth price development against the background of a shrinking market;

- **extends free allocation and indirect carbon cost compensation** beyond the current period, while free allocation is made conditional on the submission of plans to invest in decarbonisation in the EU as well as on the implementation of such decarbonisation investments in the EU;

- increases financial support to **innovation and investment** for decarbonisation, notably for industrial decarbonisation, so a higher share of EU ETS revenues is returned to sectors covered by the EU ETS. It sets up the Industrial Decarbonisation Bank (IDB) to provide **EUR 100 billion** in funding to industrial decarbonisation projects;

- extends the **Innovation Fund** in order to support the market introduction of low-carbon innovation and make clean-tech industries more competitive;

- strengthens requirements for Member States's **auction-revenue spendings**, including by introducing minimum spending on priority sectors and making visibility mandatory;

- continues to provide solidarity via the **Modernisation Fund** as a means to support the modernisation of energy systems and industrial decarbonisation in lower-income Member States, while updating the eligibility criteria and distribution key;

- continues the redistribution of **10% of auction volume** to lower-income Member States, for reasons of solidarity and channelling these resources for climate purposes;

- aims to achieve effective carbon pricing of the EU's fair share of international transport emissions through an appropriate application of the EU ETS to flights departing to the immediate neighbourhood of the Union;

- establishes dedicated, direct support to **maritime and aviation** that promotes, in particular, the uptake of EU-produced sustainable aviation and maritime fuels, clean technologies and hydrogen;

- provides for a review of the EU ETS in the event of the adoption of an IMO global measure to avoid the risk of double payments while preserving the environmental integrity of the EU ETS;

- further addresses the risk of evasion in the maritime sector through new measures and supports a level-playing field through a targeted extension of the ETS's scope to specific categories of small vessels (with a gross tonnage below 5 000 but not below 400);

- integrates **municipal waste incineration** into the EU ETS;

- secures financial means to establish an **enhanced Union Registry** that will host implementation activities and securely manage the financial instruments.

Lastly, to ensure clarity already in the ongoing period, Members States should transpose the provisions clarifying existing rules in line with their implementation and the practice by 1 January 2028.