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To:	Ms Thérèse BLANCHET, Secretary-General of the Council of the European Union
No. Cion doc.:	SWD(2026) 617 final
Subject:	COMMISSION STAFF WORKING DOCUMENT EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT REPORT <i>Accompanying the documents</i> Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Directive 2003/87/EC and Decision (EU) 2015/1814 as regards driving competitiveness and cost-effective decarbonisation REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Directive 2003/87/EC as regards revised benchmark values for the heat and fuel benchmarks period from 2026 to 2030 REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Regulation (EU) 2015/757 and Regulation (EU) 2023/1805 to simplify and streamline monitoring, reporting and verification and to align with revisions of the EU Emissions Trading System

Delegations will find attached document SWD(2026) 617 final.

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COMMISSION STAFF WORKING DOCUMENT
EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT REPORT

Accompanying the documents

Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL
amending Directive 2003/87/EC and Decision (EU) 2015/1814 as regards driving
competitiveness and cost-effective decarbonisation

REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL
amending Directive 2003/87/EC as regards revised benchmark values for the heat and
fuel benchmarks period from 2026 to 2030

REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL
amending Regulation (EU) 2015/757 and Regulation (EU) 2023/1805 to simplify and
streamline monitoring, reporting and verification and to align with revisions of the EU
Emissions Trading System

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1. INTRODUCTION

The EU has adopted a legally binding climate target of 90% reduction in net greenhouse gas (GHG) emissions for 2040 through the amendment of Regulation (EU) 2021/1119 of the European Parliament and of the Council ('the European Climate Law') compared to 1990. The target includes the possibility to use a limited quantity of high-quality international credits to make an 'adequate contribution' from 2036. This amount can be up to 5% of 1990 EU net GHG emissions, corresponding to a domestic reduction of net GHG emissions of at least 85% compared to 1990 by 2040.

To deliver the new economy-wide 2040 climate target, the climate and energy acquis for the period post-2030 needs to be revised and updated, as required by Article 6(4) of the European Climate Law. The present review of the EU Emissions Trading System (EU ETS) is the first part of a broad package of measures to deliver the post-2030 framework.

The EU ETS review assesses how the EU ETS-sectors can deliver the necessary reductions to contribute to this target in the most cost-effective way, ensuring appropriate carbon leakage protection and funding from the EU ETS revenues to support their transition, including through EU funds. Particular attention is given to industrial sectors, as well maritime and aviation. Moreover, as the size of the carbon market reduces in line with emission reductions, the review identifies how best to ensure orderly market functioning given a shrinking supply of allowances – in particular as part of the review of the Market Stability Reserve Decision.

The review also delivers on specific review clauses included in the ETS Directive and tasking the Commission to assess, inter alia, the integration of carbon removals in the EU ETS, the inclusion of waste management processes, the recognition of carbon captured and used in non-permanent products, as well as the specific review clauses of aviation and maritime provisions.

2. PROBLEM DEFINITION AND JUSTIFICATION TO ACT AT EU LEVEL

The Impact Assessment identifies two overarching problems. The first problem concerns the risk of the EU ETS not contributing cost-effectively to the EU emissions reduction target in line with climate neutrality and the 2040 target and not addressing the EU's fair share of international emissions. The second problem relates to the risk of market inefficiencies as the size of the market becomes smaller, including volatility.

In relation to the first problem, one driver is that expected residual emissions are inconsistent with the cap trajectory. As decarbonisation progresses, emissions become harder and more costly to abate, requiring additional measures, complementing the effect of the carbon price. A second driver is that sectors both inside and outside the EU ETS do not fully internalise the climate impact of their emissions, because of free allocation or because of limited coverage of the EU ETS. The third driver concerns the interaction with international carbon pricing in the transport sector, including uncertainties as regards their implementation by third countries and possible incoherence between the EU ETS and any global measures. The second problem, concerning the risk of market inefficiency, is driven by the decreasing market size as emission reductions progress towards 2040.

EU-level action is the most efficient way to address these problems. Climate change is a trans-boundary problem and both international and EU action can effectively complement and reinforce regional, national and local action. As a carbon market, the EU ETS incentivises emission reductions made first by the most cost-effective solutions across the activities it covers, achieving greater efficiency by virtue of its scale. Implementing a similar measure at Member State level would result in smaller, fragmented carbon markets, risking

distortions of competition and likely lead to higher overall abatement costs. The same logic holds for the extension of carbon pricing to new sectors.

3. OBJECTIVES

The overarching objective of this impact assessment is to ensure that EU ETS contributes cost-effectively to the EU 2040 climate target, including addressing the EU's fair share of GHG emissions.

As regards the risk of not contributing cost-effectively to the EU emissions reduction target (first problem), the impact assessment examines how to incentivise further emission reductions through EU-level funding instruments and ensuring an effective carbon price signal, including for new sectors, while addressing carbon leakage risks. It examines how to adjust the system to align it with the pre-set emissions reduction target provided by the 2040 policy package by loosening the linear reduction factor and considering how to integrate permanent carbon removals.

To support effective EU climate action on aviation and maritime emissions, the impact assessment aims to ensure that there is a meaningful carbon price on the EU's fair share of international transport emissions. It takes into account the interaction with relevant international measures, the Carbon Offsetting and Reduction Scheme for International Aviation and the upcoming global measure at the International Maritime Organisation (IMO) in the maritime sector.

As regards the risk of market inefficiencies (problem 2), the impact assessment explores ways to increase the size of the market and to adjust the MSR parameters to the decreasing market size.

4. POLICY OPTIONS

The impact assessment considers three policy options. All options align the EU ETS to the ambition of the 2040 climate target and enhance the support instruments to decarbonise accordingly. The impact assessment examines:

- if the cap follows a trajectory towards the estimated cost-effective contribution of the EU ETS to the 90% target until 2035 and then benefits from the purchase of international credits to reach the overall 2040 target by reflecting this in the estimated cost-effective contribution of the EU ETS to an 85% target from 2036-2040, or has either a linear or cost-effective trajectory from 2031 directly to a 85% emissions reductions in 2040;
- if domestic permanent carbon removals should be integrated (i) through the public or the private sector; (ii) on top of or under the cap of allowances; and (iii) subject to limits.
- different combinations of static and dynamic parameters for the thresholds to release or intake allowances into the MSR to take account of the evolution of the market until 2040;
- options to provide support to industrial decarbonisation by the Industrial Decarbonisation Bank endowed with EUR 100 bn budget. The IDB should focus on scale up and roll-out of the mature technologies and complement the Innovation Fund that will focus on innovative technologies. Options concern allocation mechanism, form of support and ways to support geographical balance;

- eliminating the possibility to finance gas and waste-to-energy under the Modernisation Fund and increasing the share of priority investments to different levels;
- options for effective carbon pricing of broader aviation CO₂ emissions (including deduction of CORSIA offsetting costs as relevant) and corresponding EU ETS-financed SAF support;
- measures to address the risk of evasion in maritime transport, deduction of emissions priced by IMO, the extension to smaller ships and support for emission reduction in the shipping sector, as well as simplification measures and the continuation of the existing derogations;
- the possibility to simplify free allocation, extend the applicable conditionalities to investments in decarbonisation, as well as the impact of phasing it out;
- the harmonization of indirect cost compensation at EU level and a strengthening of the current framework;
- the inclusion of different waste management activities in the EU ETS, and changes to point of payment for carbon that is captured and used in non-permanent products, in case municipal waste incineration is included in the EU ETS.

5. PREFERRED POLICY OPTION AND MAIN ENVISAGED IMPACTS

Overall, the impact assessment concludes that the EU ETS can be adjusted to contribute cost-effectively to the 2040 domestic climate target, while enabling a more manageable decarbonisation pathway for the EU ETS sectors with more decarbonisation options and increased financial support, and expanding to new sectors to promote effective contribution to the climate ambition by all parts of the economy. It also offers options to ensure effective climate action on the EU's fair share of international maritime and aviation emissions. The chosen preferred option corresponds primarily to PO2, with the exception of the ambition level and how removals should be integrated in the ETS, which correspond to measures CAP4 and respectively CR4:

- The EU ETS cap and linear reduction factor (LRF) are amended to contribute to the economy-wide 2040-target. This means new allowances continue to be issued into the 2040s.
- The Market Stability Reserve is reformed and better equipped to deal with scarcity situations, supporting liquidity of the market.
- Permanent domestic carbon removals are integrated in the EU ETS through the public authority, creating additional emission space for the hardest-to-abate sectors that is guaranteed and supporting the scale up the carbon removals industry, while ensuring a control of the quality and quantity of the removals.
- Free allocation and indirect carbon cost compensation are continued, while a share of free allocation is progressively made conditional on investments. In addition, the phase-out rate of free allocation for CBAM sectors is revised to account for any remaining carbon leakage risks.
- Financial support to innovation and investment in mature decarbonisation technologies is increased, including for the industry, so a higher share of EU ETS revenues is returned to businesses. In particular, the new EUR 100 bn Industrial

Decarbonisation Bank (IDB) is addressing industry. The IDB will also address the residual carbon leakage risk affecting sectors covered by CBAM.

- Effective carbon pricing of the EU's fair share of international transport emissions is achieved through an appropriate application of the EU ETS to departing flights, including avoidance of double-pricing through a deduction mechanism of CORSIA offsetting costs.
- Deduction of emissions of ships priced by IMO allows for coherence with a global measure once adopted and eliminates any risk of double pricing of emissions.
- Risk of evasion for the maritime sector is addressed by new measures.
- Dedicated, direct support to maritime and aviation promotes the uptake of EU-produced SAF, clean technologies and hydrogen and the Modernisation Fund and the Innovation Fund continue to provide substantial support.
- Municipal waste incineration is integrated in the EU ETS. The point of accounting for carbon captured in products (CCU) is placed downstream for products and at fuel producer or distributor level for e-fuels. This enables a decarbonisation route for industries with hard to abatement emissions.
- Simplification measures for the maritime monitoring, reporting and verification to reduce gaps, divergences, and duplications across existing frameworks for shipping decarbonisation.
- Targeted simplification elements benefit the industry and public authorities by reducing administrative compliance costs and enhancing the effectiveness of the system's implementation.

The **overall costs & benefits** of the preferred option cannot easily be quantified, mainly because key details will be elaborated further in delegated and implementing acts (for example reforms of carbon leakage protection measures, rules for installations in areas such CCU, carbon removal and waste, and design of the Industrial Decarbonisation Bank and ETS Investment Booster. Annex III of the Impact Assessment provides an overview of the proposal's costs and benefits, quantified to the extent possible at this stage of the legislative process.

In terms of **cost minimisation**, the proposal maintains the existing compliance framework of the EU ETS where applicable and introduces simplifications where appropriate (for example in monitoring, reporting and verification for aviation, maritime transport and stationary installations). The expansion of ETS to cover waste will build on the Directive's existing monitoring and reporting rules for this sector. In the case of carbon removal and CCU, operators will only face the relevant administration and compliance costs if they choose to make use of the proposed opportunities for reducing their surrender obligation.

In terms of **benefits**, the main benefit of the proposal is the continuation of a stable and predictable carbon price signal beyond 2030 and expansion of ETS coverage to additional sectors (waste, some aviation and maritime operators) and mitigation opportunities (carbon capture and utilisation, carbon removal).

The price signal benefit is provided by setting an ETS cap and linear reduction factor consistent with the agreed 2040 target, and reforms to the Market Stability Reserve. This in turn provides societal benefits by driving emissions reduction, innovation and investment. The proposal enhances this benefit further through new and amended uses for auction

revenues, including creation of the Industrial Decarbonisation Bank and the ETS Investment Booster and support to sustainable fuels in aviation and maritime transport. In terms of benefit to industry, the proposal also provides a more gradual decarbonisation post-2030 trajectory compared to the existing Directive, and extends carbon leakage protection measures beyond 2030, proposing reforms to the free allocation regime for industrial installations.

The scope expansion benefit contributes to meeting the economy-wide targets of the European Climate Law in the most cost-effective way possible by expanding the market-based incentive to reduce, re-use or remove CO₂ emissions to new sectors and activities