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An ETS that works for businesses and the climate

CLG Europe Position on the EU ETS review proposal

Introduction

The European Commission published its long-awaited review proposal of the EU Emissions Trading System on 17 July 2026. It is now up to the European Parliament and the EU Member States to assess the proposal, which contains significant revisions to Europe's carbon pricing system. The review is not merely a technical update to the carbon market: the choices made now will help determine whether the EU can combine decarbonisation, electrification and industrial competitiveness in the decades ahead.

The ETS should increasingly operate as both a carbon-pricing and investment framework, combining a predictable market signal with the strategic use of revenues to reduce investment barriers, lower first-mover risks and crowd in private capital for industrial transformation. Public finance should complement rather than substitute carbon pricing and private investment, helping viable decarbonisation projects reach final investment decision and commercial scale.[1] Maintaining a sufficiently strong and predictable carbon-price signal is essential not only to incentivise emissions reductions, but also to underpin investment cases and provide confidence for businesses and financial institutions.

In this paper, Corporate Leaders Group Europe gives its stance on the proposal. **We support the market-based approach of the ETS and the increased focus on its role in incentivising investment in large-scale decarbonisation projects** to achieve Europe's 2040 climate target. At the same time, the revision should recognise and support companies that make early investments in decarbonisation. Greater attention should therefore be given to mechanisms that enable and reward first movers as they undertake transformational investments across their sectors.

In addition, the European Parliament and Member States should assess the proposed reforms as a package rather than in isolation. The combined impact of different policy measures, including changes affecting investment certainty, auction revenues and industrial decarbonisation, should be considered carefully, as interactions between these measures may produce outcomes that differ significantly from those expected when each measure is assessed separately.

It is important that the revision does not inadvertently disadvantage frontrunners. Many companies have already taken investment decisions and developed climate strategies based on the expectation of a stable and predictable ETS framework. Changes to the policy design can therefore have unintended consequences for early movers and may weaken incentives for future investments

[1] This is also important for businesses outside ETS-covered sectors that rely on investment in renewable energy, electricity grids and electrification infrastructure to decarbonise their operations, logistics and transport.

in industrial decarbonisation. Policymakers should ensure that the revised framework continues to recognise and reward companies that act early in support of the EU's climate objectives.

In this context, it is essential **that the ETS review be embedded within a broader industrial decarbonisation strategy aimed at improving the underlying enabling conditions.** Without access to affordable fossil-free energy, effective carbon leakage protection, and adequate enabling infrastructures, carbon pricing alone will not deliver the intended outcomes.

This updated position builds on CLG Europe's May 2026 paper, 'A robust ETS for a competitive and decarbonised EU - CLG Europe View on the EU ETS post-2030 reform'. That initial position called for the ETS to be reinforced as a strong, cost-effective, predictable and long-term investment framework, and warned against changes that reopen agreed trajectories, reduce ambition or penalise first movers. It also stressed that the system's success depends on the broader enabling conditions that turn a carbon-price signal into real industrial transformation.

Our three key asks

CLG Europe calls on the European Parliament and Member States to ensure that the ETS remains a key driver for investment in European industry and clean electricity systems, effectively helping companies to decarbonise and ensuring that the frontrunners are rewarded for their early investments in the transition. We notably ask legislators to:

1. **Maintain the carbon-price signal and protect the integrity of the ETS**
2. **Turn ETS revenues into a real investment engine for industrial transformation**
3. **Build competitiveness through investment, electrification and innovation**

Those companies and countries still relying on fossil fuels, should not define the tempo of decarbonisation of Europe's heavy industries. Instead, we should see the ETS as an excellent lever to modernise Europe's industrial base. The European Parliament and Council will need to protect the new investment architecture while restoring a cap-and-trade design that rewards early action, crowd in private capital and keep the EU on track for climate neutrality.

Striking the right balance?

The Commission's 17 July ETS proposal and Electrification Action Plan contain important building blocks for a more coherent European energy and industrial transitions, including the proposed Industrial Decarbonisation Bank. The package recognises that businesses need both a credible carbon-price signal and the infrastructure, finance and markets that allow them to act on it.

However, the proposal does not yet fully strike the right balance. While it strengthens elements of the investment framework, it also alters key features of the ETS that have guided investment decisions to date. As policymakers consider these changes, particular attention should be paid to companies that have already undertaken significant decarbonisation investments. Many businesses have made long-term commitments and developed transition strategies based on the existing framework. The review should therefore seek to preserve investment confidence and ensure that first movers continue to be recognised and supported as they contribute to the EU's climate objectives.

This concern is shared by long-term investors, who have highlighted predictable market rules, strategic use of ETS revenues, a rules-based Market Stability Reserve and an effective CBAM as conditions for allocating capital with confidence. Recent positions from PGGM and an investor statement coordinated by IIGCC and PRI reinforce CLG Europe's view that competitiveness and climate ambition depend on a stable, investable transition framework rather than a dilution of the carbon market.

What the proposal gets (partially) right

- **A stronger investment architecture.** The ETS Investment Booster and the Industrial Decarbonisation Bank can help move mature industrial decarbonisation projects from planning to deployment. Together with the Innovation Fund and Modernisation Fund, they should address specific investment barriers – technology risk, revenue uncertainty, first-mover disadvantages and infrastructure constraints, while using limited public resources to mobilise significantly greater volumes of private capital. The headline ambition to mobilise up to EUR 100 billion is welcome, provided delivery is fast, additional and focused on measurable transformation. It will be important that these instruments schemes also cover those who have already taken concrete steps on their transformation journey.

- **More strategic use of national revenues.** Requiring Member States to direct at least 50% of relevant auction revenues towards the decarbonisation of ETS sectors is a positive step. The priority areas - including industrial electrification, clean energy, grids, storage, efficiency, circularity, lead markets and enabling infrastructure – broadly reflect the investments businesses need. The prohibition of fossil-fuel lock-in and stronger public reporting should be protected.

- **Free allocation linked more closely to investment.** While CLG Europe does not support extending free allocation beyond the agreed transition to CBAM, it is positive that the Commission has linked continued free allocation more closely to decarbonisation investment. From 2031, most recipients would need an approved, board endorsed Invest in EU Decarbonisation Plan, while the final 20% of allocation would be linked to implementation and verified emissions reductions. If free allocation is to continue, such conditions should be workable for companies, focusing on credible transition pathways and tangible progress.

- **Rules-based governance remains the foundation.** The proposal does not introduce a carbon-price cap or discretionary intervention in response to price movements. The Market Stability Reserve would continue to operate through automatic, volume-based rules. This approach is essential for investor confidence and should remain non-negotiable. The gradual inclusion of municipal waste incineration in the ETS is also a positive step. Introducing a consistent carbon price signal for incineration would better reflect the environmental cost of waste treatment and strengthen incentives for waste prevention, increased recycling and circular resource use. It can strengthen the business case for circular investments by making material recovery more competitive relative to incineration.

Where the proposal falls short

- **The cap trajectory is materially weakened.** The proposed Linear Reduction Factor falls from the current 4.4% to 3.7% in 2031-2035 and then to 1.7% from 2036, with a 2.7% fallback only if sufficient cost-effective international credits are unavailable. This would slow domestic decarbonisation precisely when energy-intensive industry needs a clear long-term signal for major investment cycles, extend the cap beyond 2040 and transfer pressure to sectors outside the ETS. Furthermore, using ETS revenues to finance international credits would mean that emitting EU-based industries help finance decarbonisation outside the EU rather than accelerating domestic transformation.

  The Commission's proposal therefore goes too far in reducing the LRF through several different mechanisms. A preferable approach would be to use the 260 $MtCO_2$ of international credits only as a safeguard and not factor the full 250 $MtCO_2$ of carbon removals into the ETS cap until there is greater certainty regarding the availability and cost of permanent removals. Uncertainty over whether the LRF will be 1.7% or 2.7% after 2036 also introduces a new source of investor uncertainty that could distort long-term decarbonisation pathways.

- **The cumulative supply effect risks recreating structural surplus.** The lower cap trajectory is combined with a reduced MSR intake rate, the proposed end of automatic invalidation, slower adjustment of thresholds, additional allowances for domestic removals and changes to free allocation. These elements should not be assessed separately. Sandbag's August 2026 scenario modelling suggests that the combined changes to the cap, removals and MSR could leave far more allowances in the market. This would weaken the carbon-price signal. While outcomes depend on how emissions and the market develop, the scale of the result demonstrates the need for transparent cumulative stress-testing.

- **International credits and removals lack sufficient safeguards.** The proposal makes a 1.7% LRF the default from 2036 and links it to the purchase of up to 260 Mt of international credits and 250 Mt of EU permanent carbon removals. Maximising the use of Article 6 credits risks turning weaker domestic action into the baseline rather than the exception. While a centrally managed facility is preferable to unrestricted operator compliance, it would still affect the ETS trajectory and revenues. By allowing part of the EU climate target to be met through reductions abroad, it could weaken incentives for domestic decarbonisation and divert public finance away from European clean technologies and industrial transformation.

  For domestic permanent removals, central purchasing, cancellation and payment on delivery are welcome safeguards. However, increasing the ETS cap by up to 260 million allowances requires stricter safeguards, including limits linked to residual emissions and a clear fallback if removals are delayed or under-delivered. Expanding the cap ex ante, without certainty that 250 Mt of EU permanent removals will be available at the expected cost, could undermine achievement of the EU's climate targets.

- **Carbon-leakage protection is prolonged.** The proposal increases free allocation for CBAM sectors by 15%, delaying the agreed transition to a full CBAM signal from 2034 to 2038. It also increases the free-allocation buffer and softens benchmark updates. This lowers auction revenues and weakens incentives for clean production and demand. A stronger CBAM, targeted support and investment conditionality should protect competitiveness without turning free allocation into a permanent substitute for transformation.

Corporate Leaders Group Europe

Three outcomes the Parliament and Council should secure

ASK 1

Maintain the carbon-price signal and protect the integrity of the ETS

The final agreement should preserve the environmental integrity and investment function of the ETS. While the Commission's proposal rightly strengthens support for industrial decarbonisation through more targeted use of revenues and conditional free allocation, its combined changes to the cap trajectory, Market Stability Reserve, free allocation, international credits and carbon removals risk creating a structural surplus of allowances.

A structurally oversupplied market would weaken the carbon-price signal and ultimately prolong the EU's dependence on fossil fuels. The ETS can only drive investment if its long-term market signal remains credible and predictable.

- **Set a stronger post-2035 emissions trajectory.** The 2.7% Linear Reduction Factor should become the default from 2036 rather than a fallback dependent on the availability of international credits. Any future adjustment should be in line with the EU's 2040 climate target.
- **Maintain a strong and rules-based Market Stability Reserve**. The Commission should demonstrate that any reduction in the MSR intake rate will not undermine the carbon price signal. Thresholds and release mechanisms should evolve alongside the shrinking market and continue to prevent both prolonged oversupply and undersupply.
- **Keep international credits out of ETS compliance.** Decarbonisation abroad can play an important role in meeting global climate goals, but it should not become a substitute for domestic industrial transformation. International credits should not be used to weaken the EU's domestic emissions trajectory or reduce incentives to invest in European clean technologies. Hence, should international credits be in any case purchased, the funds used should not come from ETS revenues.
- **Apply strict limits to carbon removals**. Permanent domestic removals should only be used to address clearly defined residual emissions and must be matched to verified delivery. Their integration should not result in a structural increase in allowance supply or weaken incentives for direct emissions reductions, especially when the availability of EU-domestic permanent CDR credits remains uncertain with the volumes and costs assumed by the Commission.

- **Assess the ETS as a system.** Parliament and Council should judge the reform on the cumulative effect of all proposed changes on the carbon market, investment certainty, auction revenues and industrial decarbonisation rather than considering individual reforms in isolation. This includes assessing the interaction between allowance supply and the investment architecture. A structurally weaker carbon price would simultaneously weaken private investment incentives and reduce the auction revenues available to finance industrial transformation. Thus, the financing architecture cannot be treated as compensation for weakening the underlying ETS signal.
- **Strengthen the signal for the circular economy.** Preserve or speed up the gradual inclusion of municipal waste incineration in the ETS, with limited scope for Member State opt-outs, to provide a consistent carbon price signal that incentivises waste prevention, increased recycling and circular resource use. This could be complemented by measures addressing landfilling of recyclable waste streams and investment in recycling and material recovery infrastructure.

ASK 2

Turn ETS revenues into a real investment engine for industrial transformation

The most positive aspect of the Commission proposal is its stronger focus on investment. A robust carbon market must be accompanied by a financing architecture that accelerates industrial decarbonisation, electrification and clean technology deployment. ETS revenues should therefore be used strategically to reduce investment risks, address market failures and crowd in private capital, rather than compensate for carbon costs or support business-as-usual production. In this context, CLG Europe welcomes the establishment of the Industrial Decarbonisation Bank (IDB) and the ETS Investment Booster.

- **Protect and strengthen the 50% investment requirement.** Member States should direct at least 50% of auction revenues towards decarbonisation investments in ETS sectors, with stronger transparency and accountability requirements to ensure funds deliver measurable transformation. Revenues should prioritise investments that reduce structural costs rather than primarily compensating for higher operational costs. Funding should focus on industrial electrification, affordable clean power, support grid users to cope with increases in grid tariffs, storage, flexibility, energy efficiency and other investments that reduce long-term exposure to fossil fuel and carbon costs.[2]

[2] For circularity, this should include investment in the infrastructure needed to scale material recovery and recycling, helping ensure that stronger carbon pricing for waste is accompanied by viable alternatives to incineration.

- **Design the IDB to unlock investment and crowd in private capital.** The IDB should act as a catalyst for investment rather than a substitute for private finance. Its support should reduce first-mover and technology risks, improve project bankability and mobilise capital from the EIB, national promotional banks, commercial banks and institutional investors. The range of financial instruments used should match different investment barriers, project maturity and risk. Its effectiveness would thus depend on its ability to unlock additional investment and move credible projects towards commercial deployment.
- **Align EU and national funding instruments into a coherent investment ecosystem.** The Industrial Decarbonisation Bank, ETS Investment Booster, Innovation Fund, Modernisation Fund, EIB financing and national support schemes should operate as complementary parts of a coherent investment ecosystem. Better coordination should reduce fragmentation, simplify access for businesses and enable projects to move from innovation and demonstration through to commercial deployment.
- **Prioritise credible industrial transition and tangible investment.** Access to support should be linked to credible decarbonisation trajectories, measurable emissions reductions and tangible capital deployment. The Invest in EU decarbonisation plans could provide an important link between free allocation, company transition planning and investment. Public support should reward implementation rather than targets that remain only on paper.
- **Reward frontrunners and accelerate investment.** Public support should reinforce, rather than replace, the carbon price signal and should progressively support technologies and projects towards commercial viability. Companies that have already invested in decarbonisation should not be disadvantaged by reforms that lower the expected return on those investments. Competitive allocation mechanisms should increasingly be used where technologies mature, while retaining targeted support where first-of-a-kind or infrastructure risks remain significant.

ASK 3

Build competitiveness through investment, electrification and innovation

The competitiveness challenges facing European industry extend well beyond carbon costs. High energy prices, labour costs and dependence on imported fossil fuels and raw materials are major structural drivers of competitive pressure.

While a lower carbon price may offer temporary relief to some sectors, it is unlikely to provide a durable competitiveness solution and may instead slow investment in the technologies that will underpin future industrial growth, while also making the EU's economy more vulnerable to future energy shocks.

- **Recognise that a weaker carbon market is not a competitiveness strategy.** Lower carbon prices alone will not address Europe's structural competitiveness challenges and risk delaying investments in clean industrial production and innovative technologies.
- **Use ETS reform to accelerate electrification and reduce structural costs.** The ETS should work alongside the Electrification Action Plan, the Industrial Accelerator Act, the Clean Industrial Deal and supporting infrastructure policies to make it easier and cheaper for companies to replace fossil fuels with clean electricity. Industrial investment and infrastructure planning should therefore not be treated separately: many industrial decarbonisation projects will only become investable where the necessary electricity, grid, transport, CO_2 or hydrogen infrastructure is available.
- **Reduce industrial exposure to fossil fuel volatility.** The best long-term protection against external price shocks is faster deployment of electrification, clean energy and efficient industrial processes rather than prolonged dependence on fossil fuels.
- **Build an investable project pipeline.** Finance alone will neither result in more competitiveness, nor resolve the shortage of mature industrial decarbonisation projects. Investment instruments should therefore combine financing with project-development assistance and technical capacity. This can help projects progress from decarbonisation plans to investment decisions and implementation.
- **Preserve the transition away from free allocation.** Carbon leakage protection remains important, but free allocation should not become a permanent substitute for industrial transformation. The agreed transition timeline towards CBAM should remain and continue to strengthen incentives for investment in low-carbon production in Europe. Continued allocation should preferably be linked to positive, incentive-based conditionality that rewards credible investments, and comes with proportional consequences for non-delivery. Europe also needs a credible solution for exports of CBAM-covered goods to maintain a level playing field in global markets. This remains a critical gap in the current proposal.

A note on ETS2

ETS2 remains separate from the post-2030 reform of the existing ETS and is not the principal focus of this paper. Nevertheless, its successful implementation will be important to the credibility and political durability of EU carbon pricing. CLG Europe supports the overall direction of extending the carbon-price signal to buildings and road transport according to the agreed timeline (2028), while recognising that these sectors face different investment barriers and distributional challenges.

Consistent with CLG Europe’s May 2026 position, successful implementation will depend not only on the carbon-price signal, but also on affordability, infrastructure readiness and social acceptance. As carbon costs are passed through fuel prices, households and small businesses must have access to affordable alternatives, including building renovation, clean heating, public transport, zero-emission mobility and charging infrastructure. The Social Climate Fund and ETS2 revenues should therefore be deployed early, strategically and transparently to unlock these investments and support vulnerable groups. Any adjustments should preserve regulatory certainty and avoid weakening the agreed framework before it has been fully implemented.

Conclusion

Europe's competitiveness challenge will not be solved by weakening the EU carbon market. Lower carbon prices may offer short-term relief, but they will not address the structural drivers of industrial competitiveness, nor will they encourage the investments needed for the industries of the future.

The ETS has been successful because it combines a clear long-term signal with the flexibility of a market-based instrument. It has already demonstrated that significant greenhouse gas reductions can be achieved while sustaining economic growth.

The review should build on that success, not dilute it. A strong ETS, combined with targeted investment in electrification, infrastructure and industrial decarbonisation, remains the best route to a more competitive and resilient European economy.

The task for policymakers is therefore clear: keep the carbon price signal strong and stable, and protect the integrity of the ETS, use ETS revenues to accelerate industrial transformation, and ensure Europe remains an attractive place to invest in clean industrial production. A stronger ETS is not a barrier to competitiveness, but its very foundation.

External references

The following public *sources informed this position and provide the basis for the policy and investor perspectives referenced above.*

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