International Carbon Action Partnership

EU Emissions Trading System for buildings and road transport ("EU ETS 2")

General Information

ETS Description

In July 2021, the European Commission proposed the “Fit for 55” package of reforms to align EU climate and energy policy with the objectives of the “European Green Deal”, most importantly the ambitious 2030 climate target of reducing net emissions to at least 55% below the 1990 level. The package included important amendments to the EU ETS framework, including a proposal to extend emissions trading to new sectors. These amendments were adopted in the first half of 2023 and are now in force.

A new, separate emissions trading system (ETS 2) will be established for emissions from fuels used for combustion in buildings, road transport and additional sectors (mainly small industry not covered by the existing EU ETS. The ETS 2 will complement other policies of the European Green Deal in the covered sectors, helping Member States achieve their emission reduction targets under the “Effort Sharing Regulation” (Regulation (EU) 2018/842).

The ETS 2 is based on the ‘cap-and-trade’ principle. It will cover emissions upstream, meaning the obligation to surrender allowances will fall on the fuel suppliers rather than end-consumers. The ETS 2 cap will be set to bring emissions down by 42% by 2030 compared to 2005 level.

The ETS 2 is due to become fully operational in 2027 (in 2028 in the event of exceptionally high energy prices). As a first step, the monitoring and reporting of emissions from the covered sectors will already start in 2025. To necessary rules were adopted in October 2023.

Allowances in the ETS 2 will be distributed exclusively via auctioning. In 2027, an additional auction volume will be front-loaded to ensure a smooth start of the system. The ETS 2 will also operate with a dedicated, rule-based market stability reserve to mitigate insufficient or excessive supply of allowances to the market.

A share of revenues from the ETS 2 will be used to support vulnerable households and micro-enterprises through a dedicated Social Climate Fund, created as part of the “Fit for 55” package. Member States will be required to use the remaining ETS 2 revenues for climate action and social measures.

ETS Status

under development

Jurisdictions

Austria
Belgium
Bulgaria
Croatia
Cyprus
Czech Republic
Denmark
Estonia
Finland

France
Germany
Greece
Hungary
Iceland
Ireland
Italy
Latvia
Liechtenstein
Lithuania
Luxembourg
Malta
Netherlands
Norway
Poland
Portugal
Romania
Slovakia
Slovenia
Spain
Sweden

Year in Review

The revision of the ETS Directive in the context of the European Green Deal and the "Fit for 55" was adopted in May 2023 and is now in force. It has introduced ETS 2 for emissions from fuel combustion in buildings, road transport and additional sectors (mainly small industry not covered by the EU ETS). A separate regulation which was also adopted in May 2023 created the Social Climate Fund, which will pool a share of revenues from the auctioning of allowances in the ETS 2 to finance decarbonisation measures and investments in the covered sectors.

In October 2023, rules for the monitoring and reporting of emissions in the ETS 2 were approved.

Sectoral coverage

Transport
Buildings

Revenue usage

Climate mitigation
Pursuit of other development objectives, such as education and health
Assistance for individuals, households, and businesses

Emissions & Targets

Overall GHG Emissions excl. LULUCF (MtCO2e)

3,468.3 (2021)

GHG reduction targets

By 2030: Reduce net emissions to at least 55% below 1990 levels (European Climate Law)

By 2050: Climate neutrality (European Climate Law)

Size & Phases

Sectors and thresholds

Fuel combustion in road transport, heating and cooling in buildings and additional sectors (mainly small industry*)

* Energy Industries (1A1) and Manufacturing Industries and Construction (1A2) according to IPCC guidelines categorization, excluding other EU ETS installations.

Point of regulation

Upstream

Type of entities

Entities releasing fuels for consumption (e.g., fuel distributors)

Allowance Allocation & Revenue

Allowance allocation

Allowances in the ETS 2 will only be auctioned. A share of ETS 2 allowances will be allocated to and auctioned for the Social Climate Fund. All remaining ETS 2 allowances will be distributed among Member States to be auctioned, based on the average distribution of emissions in the covered sectors over 2016 to 2018.

Use of Revenues

The Social Climate Fund is created alongside the ETS 2 to help EU Member States in financing structural measures and investments in energy efficiency and renovation of buildings, clean heating and cooling and integration of renewable energy, as well as in zero- and low-emission mobility solutions. Member States will also have the option of spending part of the resources on temporary direct income support.

All measures and investments will be compiled in national Social Climate Plans. The Fund will pool resources from the auctioning of allowances in the ETS 2 as well as of 50 million allowances from the EU ETS. Together with a mandatory 25% contribution of the Member States to their Social Climate Plans, the Fund should mobilise at least EUR 86.7 billion (USD 94.2 billion) between 2026 and 2032.

Member States will be required to use their remaining ETS 2 revenues for climate action and social measures.

Compliance

Compliance mechanism

Covered entities must surrender one allowance per tonne of CO_2 emitted for all their verified emissions in a compliance period.

Compliance Period

One year. Deadline for surrendering allowances: end of May every year from 2028.

Monitoring, Reporting, Verification (MRV)

MONITORING: Starts in 2025. The monitoring approach is to use scope factors to distinguish final consumption sectors and emission factors for fuel types.

REPORTING: Starts in 2025. By the end of April 2025, covered entities must submit their first emission reports for the historical emissions in 2024. From 2026, covered entities will report verified emissions based on the monitoring.

VERIFICATION: Verification of emission reports by an independent accredited verifier is required from 2026.

Market Regulation

Market Stability Provisions

The ETS 2 has been designed to start smoothly and efficiently. Over the course of 2027, a 30% higher volume of allowances will be auctioned to provide market liquidity. The ETS 2 will also operate with a dedicated, rule-based market stability reserve to mitigate insufficient or excessive supply of allowances to the market, and with measures in the event of an excessive price increase.

ETS 2 MARKET STABILITY RESERVE (MSR): The reserve will be initially endowed with 600 million allowances.

TRIGGERS: During the first three years the ETS 2 is operational, if the price of allowances exceeds EUR 45 (USD 49) (in 2020 prices, i.e. adjusted for inflation), additional allowances may be released from the ETS 2 market stability reserve to address excessive price increases. Allowances may also be released from this reserve if the price of allowances increases too rapidly, according to specific rules and conditions.

Other Information

Institutions involved

European Commission: responsible for establishment of the ETS 2 legal framework.
Competent authorities of all EU Member States: responsible for implementation of ETS 2.

Regulatory Framework

Directive (EU) 2023/959 of the European Parliament and of the Council amending Directive 2003/87/EC establishing a system for GHG emissions allowance trading and Decision (EU) 2015/1814 on MSR for the GHG emission trading system

Regulation (EU) 2023/955 of the European Parliament and of the Council establishing a Social Climate Fund and amending Regulation (EU) 2021/1060

Commission Implementing Regulation (EU) 2023/2122 updating the monitoring and reporting of greenhouse gas emissions pursuant to Directive 2003/87/EC

Disclaimer

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