

CONSULTATION RESPONSE

September 2025

The Importance of a Reformed
EU ETS State Aid Scheme
& Technical Updates to the
Emissions Trading Scheme
(ETS) State Aid Guidelines



Technical updates of the Emissions Trading Scheme (ETS) State aid guidelines – Feedback response

Bellona Europa urges the European Commission not to include additional sectors under the ETS State Aid Guidelines, particularly if Indirect Cost Compensation (ICC) continues to be allocated under the current formulas and conditions. While we recognise the importance of protecting European industry from carbon leakage, expanding the scope of ICC without addressing its structural flaws would risk undermining both climate objectives and the mechanism's original purpose. **Any expansion should be carefully evaluated and carried out by reforming the ICC to ensure it only compensates for the spillover carbon cost on the share of zero-emission electricity consumed, making it also compatible with the inclusion of indirect emissions in the CBAM across all sectors.** By reforming ICC prior to expanding its scope, the EU can maintain the measure's role in preventing carbon leakage while safeguarding ETS integrity, ensuring efficient use of ETS revenues, and supporting the broader decarbonisation agenda.

The **ICC mechanism in its current form does not distinguish between electricity from renewable and fossil electricity. Thus, it sometimes effectively acts as a fossil fuel subsidy, shielding even the most carbon-intensive electricity from the full ETS price signal.** From a climate perspective, this undermines the incentive to decarbonise power consumption. From a governance perspective, the scheme's inconsistent and non-transparent allocation across Member States creates competitive distortions and limits accountability. Expanding ICC's scope without addressing these weaknesses would exacerbate both climate and governance problems.

Additionally, the proposal requires clarification on the following aspects:

-Justification: The Commission justifies the proposed sectoral expansion by stating that "price assumptions made in 2020 no longer reflect the current market

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conditions.” If this refers to electricity price increases from the energy crisis, it is important to acknowledge that ICC is meant to protect against the carbon cost in electricity, not general price spikes. Moreover, the energy crisis affected all sectors, but energy-intensive ones originally targeted remain most exposed. However, if “market conditions” refers to factors other than the recent energy crisis, these should be clearly identified and explained

-Impact assessment: The Commission describes the changes as a “limited technical update” and states that the methods and conclusions from the 2020 impact assessment remain valid. However, this seems inconsistent with its rationale: if the market conditions have indeed changed, then a new evidence base should be required. Adjustments of this magnitude should indeed be supported by updated data and transparent analysis, especially when they risk reallocating significant public funds.

-ETS revenues: Expanding ICC would, in Bellona’s view, lead to one of these two problematic scenarios. 1) If Member States do not increase the total ICC budget, the support available for the most electricity-dependent, energy-intensive sectors would diminish. 2) if Member States increase the ICC budget to accommodate more sectors, this would mean diverting a larger share of ETS revenues away from climate action and into compensation payments, in contrast with the reformed ETS Directive agreement.

For these reasons, **Bellona Europa recommends not to expand the EU ETS State Aid scheme to further sectors under the current design.** If this expansion was to happen, compensation should be strictly limited to the share of electricity purchased and consumed that is zero-emissions but still subject to the carbon cost, ensuring that electricity from emitting sources is fully exposed to the ETS price. This would better align the ICC with the EU’s climate objectives, be compatible with CBAM’s expansion of indirect emissions and safeguard ETS revenues for their intended purpose, accelerating the low-carbon transition.

Please read the document attached for more details.

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Bellona Europa is an international, independent and non-profit organisation that meets environmental and climate challenges head on. We are solutions-oriented and have a comprehensive and cross-sectoral approach to assess the economics, climate impacts and technical feasibility of necessary climate actions. To do this, we work with civil society, academia, governments, institutions, and industries.

The importance of a reformed EU ETS State Aid scheme

Bellona Europa recognises the importance of protecting European industry from carbon leakage arising from carbon cost in electricity, but urges the European Commission not to include additional sectors under the ETS State Aid Guidelines, particularly if Indirect Cost Compensation (ICC) continues to be allocated under the current formulas and conditions. ICC must be reformed, ensuring it only compensates for the spillover carbon cost on the share of zero-emission electricity consumed, making it also compatible with the inclusion of indirect emissions in the CBAM across all sectors. By reforming ICC prior to expanding its scope, the EU can maintain the measure's role in preventing carbon leakage while safeguarding ETS integrity, ensuring efficient use of ETS revenues, and supporting the broader decarbonisation agenda.

Indirect Cost Compensation: Origins and Shortcomings

Origins and Functioning of ICC

Indirect Cost Compensation (ICC) is a state aid measure established under the EU ETS Directive, with detailed rules set in the *Guidelines on Certain State Aid Measures in the Context of the System for Greenhouse Gas Emission Allowance Trading Post-2021* or "ETS State Aid Guidelines", from now on "ICC Guidelines". ICC aims to address the risk of carbon leakage for sectors that face significant indirect costs from the EU ETS - namely, the carbon costs passed through into electricity prices.

The current aid granting period runs from 2021 to 2030. ICC is financed through ETS allowance auction revenues, with Member States allowed to use up to 25% of their annual ETS revenues for this purpose. This is an exception to the general rule in the ETS Directive that revenues should be fully directed towards climate action.

The ICC Guidelines detail the technical and procedural aspects of the measure. Here are the most relevant for this paper:

- **Formula to calculate the aid:** The standardised formula to calculate the maximum aid payable per installation links compensation to factors such as electricity consumption, production volume, local carbon emissions, and a static aid intensity (capped at 75%).

Crucially, this approach does not distinguish electricity from emitting versus non-emitting sources. (Point 28)

- **Conditions:** Large beneficiary companies need to respect either one of the following conditions: implement energy audit recommendation, consume at least 25% of renewable energy, or invest at least 50% of compensations towards greenhouse gas reduction (Point 55).
- **Transparency requirements:** the guidelines include transparency requirements to ensure public oversight of ICC. Specifically, Member States, the Commission, economic operators, and the public must have easy access to all relevant acts and information regarding aid granted. (Points 56, 57, 58).

Shortcomings of the Current ICC System

While ICC mitigates some risk of carbon leakage, its current structure undermines climate goals and presents governance issues. These shortcomings would be amplified if the scheme were extended to additional sectors without reform.

The main weaknesses are:

- **Fragmentation:** ICC are distributed by Member States in an uneven manner with some Member States making abundant use of this instrument while others not using it at all.¹ This exacerbates the differences between Member States, in a period in which industrial decarbonisation and competitiveness of the whole Union is at stake. Even though the ETS Directive specifies that “[...] the Commission shall also consider whether measures in relation to the compensation of indirect costs should be further harmonised”, for now no improvement has been made in this direction.
- **Misuse of ETS revenues:** Under the reformed EU ETS Directive, revenues generated from the auctioning of the allowances “shall” be fully allocated to climate action. However, ICC represent an exception, allowing Member States to use up to 25% of ETS revenues collected for this purpose, although ICC itself does not qualify as climate action. On the contrary, they currently function as an indirect subsidy for fossil-based power generation as well, contradicting the overarching goal of the ETS to drive decarbonisation.
- **Flawed implementation formula:** The formula in point 28 allows compensation based on fossil electricity consumption and overall output, regardless of the actual electricity mix used. This means companies using high-emission electricity are still compensated,

¹ https://climate.ec.europa.eu/document/download/92ec0ab3-24cf-4814-ad59-81c15e310bea_en?filename=2024_carbon_market_report_en.pdf In 2023, the following Member States made use of ICC: Austria, Belgium, Czechia, Finland, France, Germany, Greece, Italy, Luxembourg, Poland, Portugal, Romania, Slovakia, Slovenia, Spain.

effectively negating the carbon price signal, violating the polluter-pays principle and undermining overall EU climate objectives.

- **Weak conditions:** The conditions in point 55 of the Guidelines are minimal and only require companies to meet one of the three. Accordingly, in a hypothetical scenario where an eligible energy-intensive installation is directly connected to a fossil-based power plant and consuming 100% fossil-based electricity, it could still qualify for ICC merely by implementing energy audit recommendations, which is already part of other EU legislations. While this would align with the ICC objective of mitigating carbon leakage risks, this illogical outcome highlights how the current design of ICCs contradicts the EU climate objectives by subsidising fossil-based power production. Member States have the option to strengthen these conditions, but whether to do this or not is left to their discretion. These risks increasing disparities in implementation across the EU.
- **Lack of transparency:** Despite the transparency requirements set out in the ICC Guidelines, in practice the allocation of ICC lacks sufficient oversight. This results in unclarity as per whether the compensation accurately reflects the spillover effect of carbon pricing on electricity costs. According to the Guidelines: "Member States, the Commission, economic operators and the public must have easy access to all relevant acts and to pertinent information about the aid awarded thereunder." In reality, this information is not easy to find, making it hard for public scrutiny.

Bellona's Proposal for Reform Before Any Expansion

If the Commission proceeds with expanding ICC to new sectors, it must first reform the scheme to ensure climate integrity, competitiveness, and fairness.

Bellona recommends the following principles:

- Target only non-emitting electricity exposed to carbon cost pass-through

ICC should compensate only for the spillover of carbon costs on renewable and other low-carbon electricity, not on fossil-based electricity.

- Harmonise ICC distribution across Member States

With the introduction of the CBAM as an EU-wide policy, the European Union should address the carbon cost spillover effect on electricity prices from a Union-wide perspective, ensuring a more harmonised and consistent approach to the distribution of ICC.

- Earmark ICC spendings to climate action

Require that at least 50% of ICC received be earmarked for climate action and energy efficiency, making mandatory one of the conditions already included in point 55 of the ICC Guidelines. This would ensure effective use of ETS revenues and spending should be guided

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The logo for Bellona Europa, featuring the word "BELLONA" in a large, bold, serif font, with "EUROPA" in a smaller, spaced-out serif font below it. The text is white and set against a dark teal background that is part of a larger teal graphic element on the right side of the page.

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by clear criteria: climate impact, system effect, timing and scalability, and compliance with the Do No Significant Harm (DNSH) principle.²

- Ensure transparency and oversight of ICC allocation

Ensure that information on ICC distribution is published in a clear, accessible and standardised format across Member States. This should include the amount of aid granted per installation, justification of eligibility and documented use of ICC revenues. The Commission should monitor compliance with transparency rules and publish an annual EU-wide summary to enable effective public and stakeholder scrutiny.³

- Assess phase out ICC post-2030

Evaluate the phase-out of ICC after 2030, in line with the decarbonisation of EU electricity grid and decreasing exposure to carbon cost spillovers. As fossil-based sources increasingly cease to set the marginal price, the rationale for compensating indirect carbon costs will weaken.

By reforming ICC before expanding its scope, the EU can maintain the measure's role in preventing carbon leakage while safeguarding ETS integrity, ensuring efficient use of ETS revenues, and supporting the broader decarbonisation agenda.

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² Read more about the criteria here: [Brief.pdf](#)

³ As foreseen in the point 55 of the ICC Guidelines.