

Creating a competitive pathway to climate neutrality: Seven proposals for the EU ETS review

Executive summary

Europe's technology industries are fully committed to the target of achieving climate neutrality by 2050. The upcoming review of the EU ETS is a great opportunity to ensure a path towards that target which bolsters the competitiveness of European companies. Orgalim believes that tailored solutions must be found to better reconcile climate ambition with Europe's industrial competitiveness. EU ETS 1 has been instrumental in reducing emissions and should be a key policy measure to reach neutrality, together with ETS 2. As global competition intensifies, a recalibrated approach is needed to ensure that EU climate policy structurally supports the technologies that are essential for decarbonisation, electrification and clean manufacturing. To achieve a competitive and predictable pathway to net-zero, **Orgalim calls on EU policymakers to focus on the following seven aspects in the upcoming ETS 1 review:**

1. Create a predictable, long-term framework to achieve climate neutrality by 2050
2. Firmly establish technology neutrality as a guiding principle for decarbonisation
3. Maintain the 90% climate target by 2040, but create a more pragmatic pathway to achieve it
4. Increase the use of EU ETS revenues for innovation and modernisation
5. Re-adjust the Linear Reduction Factor (LRF) to align it with 2040 and 2050 targets
6. Delay the phase-out of free allocation for critical sectors
7. Achieve an adequate inclusion of permanent carbon removals

These steps will enhance investment certainty, rebalance efforts across sectors, safeguard industrial competitiveness and accelerate Europe's clean-tech leadership on the path to climate neutrality.

Creating a competitive pathway to climate neutrality

The European technology industries that Orgalim represents welcome the political focus on the critically important role of European industry and manufacturing in achieving the climate transition. We are global leaders in providing carbon-neutral energy, electrification and clean manufacturing technologies that are needed to achieve net-zero and a circular economy, and we are committed to playing our part.

European industry is in a delicate position, and the unprecedented wave of new green and digital EU legislation has yet to translate into widespread positive impact for our companies. The current situation regarding investments in our industries is concerning. Investments have been declining for several years, falling by 3.2% in 2024 and by 0.5% in 2025¹. An international comparison of economic indicators for manufacturing clearly shows a continuing erosion of the competitiveness of European industry. Unless the EU makes boosting competitiveness a top priority, both in words and in action, European manufacturing will continue to lose ground on the global market. This will not only put at risk Europe's net-zero ambitions, but also jobs, welfare and the standard of living of its citizens.

While Orgalim remains fully committed to achieving climate neutrality by 2050, the EU will need to adapt legislation and achieve a fairer balance between different European sectors in delivering the net-zero transformation. As a market-based, technology-neutral and cost-efficient tool, the EU ETS is a key driver for decarbonisation and investment in clean tech and has been instrumental in the green transition. In the upcoming review of EU ETS 1, the world's biggest carbon market, we therefore recommend that the EU focuses on how to reconcile European industrial competitiveness with the long-term climate neutrality goal.

¹ Orgalim Economics & Statistics reports from Spring 2025 and 2026

Seven proposals for the EU ETS 1 review

We call on EU policymakers to focus on the following key aspects in the upcoming EU ETS 1 review:

1. Create a predictable, long-term framework to achieve climate neutrality by 2050
2. Firmly establish technology neutrality as the guiding principle for decarbonisation
3. Maintain the 90% climate target by 2040, but create a more pragmatic pathway to achieve it
4. Increase the use of EU ETS revenues for innovation and modernisation
5. Re-adjust and extend the Linear Reduction Factor (LRF) to align it with 2040 and 2050 targets
6. Delay the phase-out of free allocation for critical sectors
7. Achieve an adequate inclusion of permanent carbon removals

1. Create a predictable, long-term framework to achieve climate neutrality by 2050

We support a high level of ambition in EU climate policy, fully in line with the goal of achieving climate neutrality by 2050. Our industries produce many of the cutting-edge technology solutions that are essential to achieve carbon neutrality such as: carbon-neutral energy solutions, clean manufacturing technologies, grid/electrification technologies and advanced manufacturing.

To send the right long-term signals to investors, producers, customers and other relevant stakeholders, it is important to maintain a predictable long-term framework that structurally supports investments and industrial competitiveness. Therefore, we should revise the ETS₁ to ensure a predictable path to 2040 and climate neutrality, allowing business to plan investments.

2. Firmly establish technology neutrality as the guiding principle for decarbonisation

The overwhelming priority of the EU in pursuing decarbonisation must be to reduce greenhouse gas emissions in a technology-neutral manner. This means that technology neutrality should be guiding all EU initiatives on climate action. The EU should rely on market-based systems in the search for climate-friendly solutions and specific technologies should not be favoured as long as the most cost-efficient pathway towards carbon neutrality is also incentivised when it comes to research. This is particularly important in the fields of energy efficiency, electrification and sustainable product development.

3. Maintain the 90% climate target by 2040, but create a more pragmatic pathway to achieve it

Orgalim supports the intermediary 2040 EU target of 90% net emission reduction in the Revised EU Climate Law. An intermediary target is a cornerstone of a stable and predictable long-term framework to reach climate neutrality. It will help to attract and channel investments into low-carbon technologies and establish cost-effective policies supporting our industries' innovative drive and boosting the competitiveness of our low-emission products, services and technologies. As such, a clear and ambitious climate target can also act as a comparative competitive advantage in global markets. In addition, it can help Europe maintain leadership in international climate negotiations. **However, it is necessary to create a more pragmatic pathway to rebalance the effort that is required from different sectors by 2040. It is therefore important to have a fully operational EU ETS 2.**

4. Increase the use of EU ETS revenues for innovation and modernisation

Furthermore, there is also a need to increase support for innovation in decarbonisation technologies and the modernisation of European industry. Orgalim therefore calls for an increased amount of the revenue from auctioning ETS 1 allowances to be dedicated to the Innovation Fund and the Modernisation Fund. The Innovation Fund should continue working under excellence criteria, with more than 5% of the EU ETS allowances revenue to be used to cover its funding. Moreover, the Innovation Fund should focus on supporting technologies that have not yet been fully commercialised. The Modernisation Fund works like a cohesion fund and should also have its funding increased to over 3% of the EU ETS allowances. The overall functioning of these funds should be optimised with a view to the various new schemes introduced under the Clean Industrial Deal and the AccelerateEU initiatives.

5. Readjust and extend the Linear Reduction Factor (LRF) to align it with 2040 and 2050 targets

EU ETS 1 has a cap for the total number of allowances released on the market that drops each year. Under the current trajectory, ETS 1 is already set to reach zero by 2039. Accordingly, there is space to decrease the pace of reductions in carbon allowances each year (set by what is known as the Linear Reduction Factor, LRF) and still meet the EU's 2040 and 2050 climate targets.

- **We recommend to adjust the LRF to achieve a more pragmatic pace for industry (while remaining aligned with the overall trajectory to achieve a 90% reduction by 2040 and climate neutrality by 2050).**
- **In particular, we propose a 90% reduction compared to 2005 (when the system was launched) which would mean that the current rate of reducing allowances of more than 4.4% should be lowered so that EU ETS 1 reaches carbon neutrality by the mid 2040's.**

Any adjustment should maintain the integrity of the ETS as a driver for decarbonisation and achieving the EU's climate targets. The EU ETS 1 review should be accompanied by a state of the art impact assessment covering the economic impact on society, industry and investments in clean technologies.

While this would mean that the LRF beyond 2040 would be lowered, it would still mean that EU ETS 1 would be carbon-neutral by the mid 2040's and thus well before the carbon neutrality target in 2050. Together with other parts of the revision this will ensure the necessary ETS 1 liquidity to support future key investments.

6. Delay the phase-out of free allocation for critical sectors

The suggested phase-out of free allocation of allowances in EU ETS 1 for CBAM-covered sectors by 2034 will put severe pressure on several sectors that are exposed to fierce international competition. **We therefore call for a pragmatic delay in the phase-out of free allocation and the phase-in of CBAM.** This policy option would temporarily lower the cost of carbon neutrality for critical sectors in EU ETS 1 and the price for CBAM imports, while maintaining the long-term incentive to decarbonise. With a lower LRF in EU ETS 1, there are increased possibilities to delay the phase-out of free allocation and the phase-in of CBAM.

The time gained must be used to urgently and thoroughly improve the CBAM instrument, ensuring protection against carbon leakage and maintaining competitiveness within the EU and third-country markets. This must apply not only to ETS 1 sectors, but also to downstream industries.

7. Ensure an adequate inclusion of permanent carbon removals

Orgalim **supports the inclusion of domestic technical permanent carbon removals credits** in the EU's cap and trade system for greenhouse gases, the EU ETS, and in the emission reduction calculation. Orgalim recommends that the European Commission ensures that the carbon removal framework and revised ETS are aligned as a further step in supporting the development of a robust carbon dioxide removal (CDR) market within Europe. Finally, it is crucial to establish a clear and predictable volumetric on-ramp for CDR into the ETS. Such steps could help strengthen and scale the European removals technology market, as currently available solutions are financially challenging and lack adequate funding, thereby enabling more project developers to enter the market while expanding the pool of potential buyers.

Links to Orgalim publications

- [Orgalim Policy Agenda](#) for a European high-tech manufacturing base
- Orgalim's statement on [the climate law](#)
- Orgalim's position on the [2040 climate target](#)
- Orgalim's [key recommendation on energy and climate](#)

Short explanation of EU climate policy tools

This list (which is not exhaustive) explains some of the major EU climate policy tools.

EU ETS 1 (EU Emissions Trading System – main scheme)

The EU ETS 1 is the EU's cap-and-trade system covering power generation, heavy industry, and the intra-EU aviation and maritime sector, where companies must hold allowances for every tonne of CO₂ they emit. The cap decreases annually, making emissions progressively more expensive and driving decarbonisation efforts.

EU ETS 2 (new ETS for buildings, road transport and small industry — starting 2028)

EU ETS 2 creates a separate carbon market for fuel suppliers to buildings, road transport and certain smaller sectors, making fossil fuel use more costly across the economy. It introduces a gradually tightening cap and a price-stabilising mechanism to avoid excessive volatility.

LULUCF (Land Use, Land Use Change and Forestry Regulation)

LULUCF sets rules for how Member States must account for carbon removals from forests, farmland and other land use activities. The regulation requires the EU to increase its carbon sink by 2030 and ensures that land use emissions do not exceed removals.

CBAM (Carbon Border Adjustment Mechanism)

CBAM applies a carbon price on certain carbon-intensive imports (e.g. steel, cement, fertilisers) to prevent "carbon leakage" and ensure fair competition as the EU tightens its own climate policies. Importers must purchase CBAM certificates reflecting the embedded emissions unless they can prove the carbon price was already paid in the country of origin.

Orgalim represents Europe's technology industries, comprised of 770,000 innovative companies spanning the mechanical engineering, electrical engineering, electronics, ICT and metal technology branches. Together they represent the EU's largest manufacturing sector, generating annual turnover of over €2,972 billion, manufacturing one-third of all European exports and providing over 11,9 million direct jobs. Orgalim is registered under the European Union Transparency Register – ID number: 20210641335-88.

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