

CARBON GAP'S POSITION PAPER ON CARBON REMOVALS IN THE EU EMISSIONS TRADING SYSTEM (JUNE 2026)

This document outlines Carbon Gap's positioning on the three policy options for integration of carbon dioxide removals into the EU Emissions Trading System as outlined by the European Commission on 12 May.

SUMMARY OF CARBON GAP'S POSITION

The 2026/27 review of the EU Emissions Trading System (ETS) ¹ is a **critical opportunity for creating a large-scale market demand signal for carbon dioxide removal (CDR) in the EU**. The ETS integration is unrivalled in terms of the potential scale of impact on the CDR landscape. Despite the EU recognising that CDR plays a clear role in its path to climate neutrality, there are no other policies under consideration in the EU that could potentially deliver CDR at megatonne scale and over decadal timeframes.

Yet while the ETS review is an important lever for supporting CDR, success will be determined by the details of policy design. The ETS has not been designed to support CDR, and has flaws as a potential market to drive CDR to [needed scales](#) (which are in the range 75-280 MtCO₂e/year by 2040). Some of the key issues include price gaps between expected EU allowance (EUA) prices and CDR costs, scope limits (polluting sectors that should pay for CDR but that are not fully covered by ETS), and a declining ETS cap (contrasting with the need for growing CDR demand). Careful policy design is needed to overcome these barriers while maintaining the core function of the ETS.

CDR integration is not without risk. Proposals are coming forward during a period of increased “flexibility” in climate target design. Yet CDR is already part of the base case for EU decarbonisation. Any use of CDR as a flexibility for the ETS comes **over and above existing EU CDR needs**. Relying on CDR to buffer a more lenient ETS is an expensive and unsustainable approach to policy design.

The Commission has laid out three policy options for CDR integration. Each of these has risks and benefits in terms of EU CDR scale-up and ETS integrity, and are explored at further length in this paper. A summary of each option is provided in Table 1.

Table 1: The three options to be assessed in the Commission's Impact Assessment as outlined on the 12 May.

Public authority integration – above the cap	Operator integration – above the cap	Direct integration – with one-in-one-out
A public authority would purchase CDR credits, retire them, and issue (a corresponding amount of) EUAs into the EU ETS. Purchased CDRs would add to the overall number of allowances in the ETS.	ETS obligated entities would purchase CDRs, have them certified, and then get credits that can be surrendered to fulfil their ETS obligations. Purchased CDRs would add to the overall number of allowances in the ETS.	ETS obligated entities would purchase CDRs, have them certified, and then get credits that can be surrendered to fulfil their ETS obligations. For each CDR purchased and surrendered, an EUA would be removed from the system, meaning CDRs do not add to the overall number of allowances.

Carbon Gap supports a public authority-led “integration” of CDR into the ETS. A public authority integration would:

- Afford the European Commission control over the quality and quantity of CDR used in connection to the ETS, including the portfolio of CDR technologies deployed;
- Provide timely and large-scale demand for CDR where a “leave it to the market” operator integration/direct integration may not;
- Provide certainty about CDR volumes in the market. Target volumes could be defined as a range – with an upper bound to limit mitigation deterrence risks and a non-zero lower bound to send a clear market signal for CDR sector;
- Limit complexity for ETS covered sectors, which will continue to see EUAs only in the market, and enable alignment between conflicting accounting logics seen in ETS versus the Carbon Removal and Carbon Farming Regulation (CRCF).

However, some key issues remain unresolved in a public authority integration, which additional policy efforts must address.

- While ETS revenues can be used towards CDR purchases, **there remains a “price gap”** between the cost of many CDRs and ETS price trajectories, requiring additional support at EU or Member State level.
- The Commission's plans to use CDR “on top of” the ETS cap must be taken with a grain of salt, and a **“one-in-one-out” model should remain on the table, even if partial, to maintain climate integrity**.
- With the Commission planning to use international credits to provide ETS “breathing space”, there is a need for a clearer hierarchy of options. **Domestic CDR must be prioritised over international credits**, to avoid longer term cost lock-ins and novel dependencies to other countries. Where international credits are used, CDR must be a priority.
- The EU must now **address the wider question of how to build a long-term competitive market for CDR**, which involves grappling with questions related to the scale and frequency of public authority procurement rounds, how to set relevant purchase prices for those rounds, how to manage price competition between methods, and how to bring covered entities (CDR buyers) and CDR suppliers closer together over time.

1. PUBLIC VS PRIVATE? INTEGRATION SHOULD BE MEDIATED BY A PUBLIC AUTHORITY WHICH IS BETTER PLACED TO DEVELOP THE MARKET AT THE EARLY STAGES

What are the policy options on the table?

Core to the discussion on CDR in the ETS is whether the market is mediated by an intermediary body, or whether CDRs are traded more directly between suppliers and buyers. As shown in Table 1 above, on 12 May, the Commission laid out two different options under consideration for its legislative proposal.

- A. **Public authority integration** – Buying removals via a public authority and issuing (a corresponding amount of) allowances into the market.¹
- B. **Operator integration & Direct integration** – ETS obligated entities buy removals directly from CDR providers, have them certified, and then get CDR credits that can be surrendered to fulfil their ETS obligations. (We explore how the two options may differ in their cap interactions in the next section.)

What are the risks and benefits of each?

Table 2 compares Operator integration and Direct integration against Public authority integration. While Operator integration and Direct integration also differ in terms of the ETS cap, that matter is dealt with in the next section.

Table 2: Arguments for and against Operator integration/Direct integration and Public authority integration.

	Key arguments for	Key arguments against
Operator integration & Direct integration	➤ Promotes greater cost-efficiency via market forces, bringing buyers and suppliers closer together. ➤ Reduces administrative burden on government as ETS entities coordinate their own CDR purchasing. ➤ Could theoretically be combined with a CDR quota or sub-mandate to enhance volume certainty.² ➤ Creates a direct relationship between ETS entities and CDR suppliers, could potentially allow for inssetting/waste to energy companies to generate their own removals.	➤ Risks delivering no integration or very slow integration, given prices of CDR are currently much higher than ETS – unless a subsidy instrument is deployed to bring price parity. ➤ Even where price parity can be achieved (i.e. in the case of the UK where a CCfD is used), operator integration could lead to limited CDR demand, due to the extra administrative burden operators will face in sourcing CDRs over EUAs.² ➤ Likely to lead to a least-cost portfolio of CDR methods, hampering the ability of a more diverse and sustainable set of methods to come forward. Could create pressure to expand the set of eligible methods beyond permanent CDR, as covered entities seek more cost-effective options for hedging. ➤ Entails less control over CDR volumes and introduces further complexity for managing supply of CDR into the ETS.³
Public authority integration	➤ Drives more timely demand, with CDR procurement potentially beginning as early as 2031 or even before. ➤ Drives more reliable demand at scale, as the authority would determine centrally what an appropriate volume of CDR might be. ➤ Better able to promote a portfolio of CDR methods, including those that are not yet cost-competitive – creating a market pull for a range of methods to come forward in the EU. ➤ Centralised procurement offers greater ability to control supply of CDR into the ETS. ➤ Could allow for the procurement of different methods for other use cases than the ETS, or to allow for gradual integration based on best scientific evidence, technological maturity, or other relevant criteria.	➤ Could lead to inefficiencies, administrative burdens and thus higher costs, especially over the longer term. ➤ Public authority may have excessive price-setting power and would assume price risk associated with bridging the price gap between the strike price and the ETS price. ➤ Could stifle innovation since direct CDR project interaction with ETS covered entities is not foreseen. ➤ Could lead to unfortunate outcomes by “picking (the wrong) winners.” ➤ Requires a significant and secured source of financing.

What is Carbon Gap’s policy ask?

- **Integrate CDR via a public authority** to ensure clear demand signals that can effectively drive CDR scale-up, while giving better control over the quality and quantity of CDR integrated into the ETS.

¹ Carbon Gap’s preference is to keep this ratio one-to-one, and dealing with any inequivalences at the certification level. Introducing conversion rates between EUAs and CDRs risks further market fragmentation.

² Hence [our call](#) in the UK for a CDR “sub-mandate” or quota that mandates covered entities to buy a certain amount of CDR.

³ The UK government has proposed supply controls for direct integration, though it is unclear exactly how these would be enforced.

- Reserve the **option to transition from public authority integration to operator/direct integration in the long-term**. While more market control and political steering is likely necessary in the near-mid term, the ETS could eventually transition towards higher levels of market forces over time to drive down prices.
- **Enable long-term market making**. The public authority will help promote a more level playing field in the near term while CDR is nascent. But ETS policy should eventually aim to create a competitive market for CDR in the long term, which will in turn reduce the need for public support and uphold polluter pays. Regular procurement rounds will be needed rather than a one-off auction. The Commission must set out how CDR procurement prices will be set to ensure sufficient competitiveness and limit market distortion. An eventual move towards an operator-led integration could be helpful in promoting competition.
- **Secure pathways for wider private sector engagement with the public authority in the near-term**. Ensure that learnings from (voluntary) private sector engagements on CDR drive efficiencies within the pending public authority. In practice, such an approach could mean collaboration with private (accredited) Validation and Verification Bodies (VVBs) and/or the potential for the public authority to source CDR volumes from secondary markets⁴.
- **Position ETS integration as part a wider set of measures** to scale the EU CDR industry, driving demand for a portfolio of methods to deliver on EU climate targets.

⁴This approach could mean optionality for voluntary (but ETS-eligible) CDR purchases by private actors to be converted into EUA-compatible credits via the public authority and secondary market trades.

2. ABOVE OR BELOW THE CAP? INTEGRATION SHOULD HAPPEN BELOW THE CAP TO THE GREATEST EXTENT POSSIBLE, RECOGNISING THAT THIS IS NOT A BINARY CHOICE

What are the policy options on the table?

Policy discussions have considered how the inclusion of CDR relates to the overall availability of allowances in the ETS (the cap). Two broad options have been laid out.

A. Integrating below the cap (one-in-one-out)

- **What is it?** CDR is included within a pre-planned emissions cap and does not increase gross emissions in the system as defined by the cap.⁵
- **How is it done?** This can be done through a one-in-one-out approach – removing an EUA for each CDR (or CDR-backed EUA) added to the system.⁶
- **What is the outcome?** If and where CDR is integrated below the cap, cumulative emissions to the atmosphere are not increased as long as the CDRs used are of equivalent permanence to the neutralised emission.

B. Integrating above the cap

- **What is it?** CDR is used to relax the cap, by providing additional allowances to the system – increasing gross emissions but theoretically maintaining net emissions.
- **How is it done?** This can be done through additional auctions, the Market Stability Reserve (MSR), or other means. It is generally considered a “flexibility” approach.
- **What is the outcome?** If and where CDR is integrated above the cap, the availability of CDR leads to more allowances in the system and therefore more emissions on a gross basis.

To some extent the difference between “above the cap” and “below the cap” is semantic and not binary, since the cap post-2030 is not yet defined. If integrating CDR below the cap, the Commission is likely to account for CDR as it sets its cap level, meaning the existence of CDR may place some upwards pressure on the cap in both options. The choice will also be informed by the extent of cap relaxation happening elsewhere in the system (most likely as a reduction to the Linear Reduction Factor).

What are the risks and benefits of each?

Table 3: Arguments for and against integration above and below the cap.

	Key arguments for	Key arguments against
Above the cap: Operator integration & Public authority integration	➤ Provides “breathing space” to industry and aligns with the European Climate Law agreement where CDR is introduced as additional “flexibility.” ➤ Preferable to relaxing the cap <i>without</i> using CDR. ➤ Preferable to relaxing the cap based on international credits. ➤ Helps with the financing picture by generating additional ETS revenues through above-the-cap auctions, reducing competition for existing ETS revenues to fund CDR ➤ Separates CDR scale-up trajectory from the declining ETS cap trajectory.	➤ Potentially weakens carbon price by increasing supply (this is dependent on CDR volumes added). ➤ Any CDR under-delivery drives mitigation deterrence by allowing additional gross emissions that are not balanced by CDRs. ➤ Fails to address hard-to-abate emissions within ETS sectors (as CDR supply is instead used for breathing space). ➤ Breathing space is likely to be created through other channels.
Below the cap/ one-in-one-out: Direct integration	➤ Limits mitigation deterrence risk if CDR underdelivers. ➤ Contributes to a stronger ETS price signal. ➤ Promotes the use of CDR to address hard-to-abate emissions.	➤ Does not address the need for ETS “breathing space.” ➤ Relies on financing CDR through existing ETS revenues, rather than creating a new source of finance (through additional auctions). ➤ Constrains potential CDR demand to the (declining) cap level – a “cap switch” would likely be needed in future to be compatible with net-zero (see below). ➤ Differences may be semantic (see above) – what matters is the overall ambition across the whole ETS design.

⁵ This option is of course strongly influenced by the level at which the cap is set post-2030 – a highly contested topic politically that goes beyond CDR integration. The Commission has indicated that the post-2030 cap will not decline as aggressively as is currently planned and will remain positive in 2040.

⁶ Practicalities for implementing one-in-one-out may depend on the general policy design discussed in Section 1.

What is Carbon Gap's policy ask?

The core benefit of CDR integration in the near term is to nurture more demand for removals, build up market infrastructure, and channel ETS revenues towards CDR scale-up, while not disturbing the existing ETS reduction trajectory. Eventually, as we converge towards “residual” levels of emissions, CDR availability could be used to modify the ETS cap and allow a net-zero ETS. But for the near- to medium-term, the ETS must stay on course as an emissions reduction instrument.

While integration above the cap presents politically desirable “breathing space”,⁷ this comes at significant climate risk. It allows added gross emissions at a point when EU industries should still be prioritising reductions, and could weaken the ETS price signal. The exact level of these impacts depends heavily on design (CDR methods allowed, whether supply controls are used), but early [evidence](#) suggests mitigation deterrence effects could arise.

We recommend **integrating below the cap as much as possible** to ensure alignment with EU climate neutrality. Above-the-cap integration should thus be reserved for the longer term (see below). We also urge the Commission to **consider a public authority integration below the cap**, which was not included in the three options presented on 12 May (see Table 1). This option would offer the best management of mitigation deterrence risk. When considering CDR-ETS cap interactions, policymakers should also consider the following:

- **The relationship between cap changes and CDR** – Policymakers must decide whether any cap increases will be backed by CDR (fully, partially, or not at all). Ideally any cap increases (if they must be introduced) would be backed by CDR and would be strictly limited in volume.
- **Upper limits** – Policymakers must consider the availability of sustainable CDR volumes over time, recognising CDR as a limited resource. An upper limit of CDR to be used within the ETS must safeguard that expected CDR volumes reflect the expected scarcity of CDR volumes, safeguarding against unsustainable mitigation deterrence.
- **Lower limits** – Certainty on the minimum amounts of CDR to be used via the ETS would give project developers much needed demand clarity. The ETS integration should involve a clearly specified lower bound limit for volumes of CDR to be integrated.

Finally, an above-the-cap integration could be better suited to the ETS in the longer term because a declining cap will eventually put pressure on CDR market growth under the ETS. A “cap switch” will therefore be needed eventually – likely in the 2040s – to allow a stable volume of CDR to be used under the ETS as part of a net-zero system.⁸ This approach should not be done until there is more certainty about CDR supply and appropriate supply controls in place.⁹

⁷ Albeit at a cost to the Commission in the form of potential CDR subsidies.

⁸ Grantham Research Institute on Climate Change and the Environment (2026, forthcoming).

⁹ The UK government has also recognised the benefits of a switch from a one-in-one-out approach to an above-the-cap integration in the longer term, for these reasons.

3. BRIDGING THE PRICE GAP: THE COMMISSION MUST CLEARLY DEFINE HOW THE PRICE GAP WILL BE ADDRESSED THROUGH AVAILABLE FUNDING INSTRUMENTS

What are the policy options on the table?

The price gap between EUAs and CDR must be addressed through the strategic reinvestment of EU ETS revenues. Several sources may be relevant for funding CDR purchasing, though each with distinct political and technical obstacles to accessing them. To allow for a strategic reinvestment of EU ETS revenues for European industries, we suggest retaining a dedicated share of EU ETS revenues to be used towards CDR development.¹⁰ Below we outline the options available.

- A. **ETS revenues directed towards the EU** can be redirected towards CDR. This can be done by targeting existing ETS-funded instruments such as the **Innovation Fund**. In 2024, [close to 6%](#) of total ETS revenues went to the EU Innovation Fund. A share of these revenues must be explicitly set aside for investments in CDR through a dedicated programme or envelope under the Fund at the European level. The EU could establish a dedicated CDR track under the Fund, that could work hand in hand with ETS integration to fund large-scale projects. The proposed Industrial Decarbonisation Bank could be a further opportunity to support CDR using ETS revenues.
- B. **ETS revenues directed towards Member States** can be used more effectively to support CDR. Currently, Member State ETS revenues must be entirely directed towards energy- and climate-related spending (including carbon removal), but actual spending currently suffers from poor transparency. The Commission has indicated that strengthening disclosure and better directing the use of revenues could form part of the 2026 review. To better support CDR, Member States could spend ETS revenues on CDR procurement, providing state-backed subsidy schemes or loans from national or regional investment banks, or coordination to support Important Projects of Common European Interest (IPCEIs). This spending would likely be aligned with national climate targets in any case since most Member States anticipate using CDR to achieve their goals.
- C. In addition to the more effective use of revenues, **both the EU and Member States must establish** an investable policy framework for CDR. The CDR ecosystem is in need of public support for the foreseeable future. Today, many public investment frameworks exclude CDR or are not explicit about the eligibility of CDR within them. Investment is further stymied by factors spanning from unclear corporate claims rules to misaligned State Aid and block exemption rights. To leverage greater private sector co-investment, the EU must urgently establish an investor-friendly policy framework, namely by:
 - Aligning state aid rules and the General Block Exemption Regulation (GBER) to the realities of the nascent CDR industry;
 - Amending the GBER to include a CDR block exemption for aid below a defined threshold, e.g. €100-200m per project;
 - Updating the Climate, Energy and Environmental Aid Guidelines to create a dedicated CDR track;
 - Using the Clean Industrial Deal's strategic framework to pre-approve CDR as a priority sector;
 - Applying the Renewable Energy Directive's accelerated permitting regime to CDR as part of renewable go-to areas.

What is Carbon Gap's policy ask?

To align with EU climate neutrality goals, both the EU and Member States should direct a **gradually increasing share of ETS funding to supporting CDR** to address residual emissions, while also building an investable policy framework for CDR through updates to state aid rules and permitting regimes.

¹⁰ Notably, in a “below the cap” CDR integration, CDR reduces the ETS revenues directly available to Member States, with funds channelled towards CDR (either directly through ETS operators or via a public authority). In the longer term, this method of integration would present substantially less revenue to Member States compared to an above-the-cap integration, presenting a clear incentive for Member States to challenge below-the-cap integration (complementing existing industry calls for breathing space). Carbon Gap sees this as an inherent design feature of a successful carbon pricing system, with revenues declining predictably as the economies have transitioned towards a greener economy. While CDR integration below the cap is set to accelerate the impact felt on the public purse, via a faster paced elimination of EUAs, loss of revenues should not be a basis for reduced ambition in the ETS.

4. METHOD ELIGIBILITY: CDR METHODS RELEVANT FOR THE ETS MUST HAVE ROBUST MONITORING AND LIABILITY, UNDERPINNED BY RELIABLE LONG-TERM GOVERNANCE

What are the policy options on the table?

At the 12 May roundtable, the Commission explicitly earmarked BioCCS and DACCS for integration into the ETS, implicitly excluding other methods. Nonetheless, the Commission has also outlined plans to link the ETS to the CRCF, creating clear leverage for further “permanent removal” methods to be potentially included. This risk is compounded by a strong financial incentive to integrate biochar as a much lower-cost CDR method when compared with BioCCS and DACCS. The inclusion of biochar and further CDR methods is likely to be a lightning rod issue in the ETS review debate.

What are the risks and benefits of expanding beyond BioCCS and DACCS?

In our statement at the final CRCF expert group on permanent CDR, Carbon Gap highlighted inadequacies in the biochar methodology and called for continuous improvement. In particular, we identify discrepancies with the requirements and logic of the CCS Directive relating to long-term monitoring and liability. EU rules for CCS-based storage operators stipulate rules for monitoring (including frequency, technologies to be used, issues to look out for) and liability (including remediation strategies where issues are detected, and an eventual transfer of liability to the state). By contrast, no monitoring provisions are in place for biochar under the CRCF beyond the year following application to soil. This gap is addressed in the CRCF through a conservative discounting of creditable volumes.

Lack of monitoring and liability provisions are not the only issues facing biochar. The evidence for its permanence is not well developed, with many studies assuming biochar’s permanent fraction behaves indistinguishably from inertinite – yet this analogy has a number of issues [already outlined](#) by Carbon Direct. Modelling [suggests](#) if biochar is included in the ETS it would dominate over other CDR methods given its relative cost.

What is Carbon Gap’s policy ask?

- **Prioritise other demand signals.** Given these gaps, we do not see the biochar methodology as being, at present, satisfactory for ETS inclusion on a like-for-like basis. Our preferred option is an alternative demand signal for biochar such as a public purchasing programme.
- **Introduce additional ETS eligibility requirements.** The ETS must apply its own eligibility requirements for CDR methods until such gaps are addressed within the CRCF framework. A clear legal benchmark of quality is needed to determine what is appropriate for the ETS. It should build on specific monitoring and liability requirements aligned with the CCS Directive.
- **Target a balanced CDR portfolio.** To ensure cost-effectiveness, public authority purchases will likely be managed through competitive allocation rounds (e.g. reverse auctions). But with technologies at different TRLs today, methods will not be able to compete on a level playing field in the near term and DACCS will likely not be integrated. In the early phases, procurement tenders should be organised in buckets to ensure portfolio diversity, moving towards fuller price competition over time.

Box 1: Using the Carbon Removal Carbon Farming Regulation in the EU ETS and the question of gross vs net integration

In February 2026, the Commission adopted three methodologies for certifying permanent CDR under its Carbon Removal Carbon Farming (CRCF) Regulation. The ETS integration of CDR is a natural opportunity to use the CRCF framework – with the Commission saying on 12 May that the CRCF “will clearly play a role for ensuring quality” in the ETS. The use of CRCF could simplify the market for CDR suppliers, who may wish to trade simultaneously in the voluntary carbon market and the ETS, allowing them to use the same methodology for both.

However, there are challenges aligning logics of the CRCF and the ETS. The former relies on lifecycle-based project accounting over the entire project lifetime (“gross” accounting), whereas the latter follows an installation-based inventory accounting logic on an annual basis (“net” accounting). At the interface of the two logics, there could be important gaps or overlaps. Two key challenges include (1) the potential “double” reporting of emissions, where emissions already subject to ETS obligations are deducted under the CRCF’s “net” accounting and (2) the reporting of reversal events.

Managing potential double penalties/exposures

CDR stakeholders have argued against double exposures, which could potentially impact CDR project economics. Theoretically, if accounting overlaps are addressed (exempting ETS-covered emissions from CRCF deductions), a share of CRCF-compliant credits could be handed back to developers. (See Chapter 5.2.1 [here](#) for a more detailed discussion of how this could happen.) However, such changes would rely on an assumption of equivalence between an emission covered by the ETS and an emission deducted under the CRCF GHG_{associated} calculation (it is not within the scope of this paper to evaluate whether that equivalence holds).

Revisions may be needed, either at CRCF or ETS level, before the two systems can fully align. Carbon Gap’s view is that, at minimum, there must not be any gaps in emissions accounting. The CRCF’s cradle to grave life-cycle assessment (LCA) boundary is intended to be comprehensive, meaning no emissions should be left unaccounted for as long as the specific CRCF methodology lives up to these principles in practice. We therefore tentatively favour a net accounting in the near term via the CRCF. As evidence evolves, harmonisation of accounting could happen, perhaps by revising the CRCF methodologies over time to better align with the ETS.

Alternatively, a public authority integration potentially allows for the correction of such discrepancies within individual methodologies (at the project level) as well as for the entire scope of project methods (at the activity level). Future legislation should allow for such corrections to be handled, such as via the use of delegated acts as dynamic revisions.

Liability for managing reversals

Aligning the CRCF and ETS also relies on assurances that units (EUAs and CRCF credits) deliver similar climate benefits and can thus be treated fungibly. (Conversion ratios offer an alternative solution but are not preferred as they create complexity.) Different approaches to managing reversals currently undermine this fungibility. While the CRCF's BioCCS and DACCS methodologies leverage the CCS Directive - requiring storage to be monitored and EUAs to be surrendered where reversals occur - the same is not true for biochar, where no monitoring is required and there is no liability regime. These points should also be addressed as the CRCF evolves.

5. INTERNATIONAL CREDITS: THESE ARE NOT A FIRST-CHOICE OPTION FOR THE ETS, BUT IF THEY MUST BE USED, A CLEAR HIERARCHY WITH DOMESTIC REMOVALS IS NEEDED

What are the policy options on the table?

In line with the ECL, international carbon credits will play a role in achieving the 2040 climate target, and in turn could be (re)introduced to the EU ETS. Phase 2 of the ETS (2008–2013) already saw high volumes used directly by obligated entities. Their environmental integrity and economics, however, were seen as predominantly [negative](#). As the EU reopens to Article 6 credits as a new form of international cooperation, any role for international credits in the ETS deserves careful attention and good design. Three routes for international credits in the ETS are emerging:

- A. Direct use as a compliance instrument,
- B. Use to provide breathing space to the ETS,
- C. Limited use to provide hedging in the case of unforeseen domestic underperformance.

We welcome the Commission's caution towards Option A and agree international credits **should not be eligible to fulfil ETS compliance obligations**. Nevertheless, the Commission has kept a separate, indirect linkage on the table: namely, the ETS cap could be given additional breathing space backed by international credits. We suggest that international credits should only play a limited role, doing so could provide breathing space in the case of unforeseen and unplanned circumstances only, in line with Option C. Notably, they could serve as a tool to expand the availability of pCDR for European targets, where unforeseen barriers prevent a fully domestic target achievement. Such use must be made conditional on other performance indicators, enabling their limited use as an emergency hedge. This approach compares favourably to a reliance on international credits to reduce ETS ambition from the outset.

What are the risks and benefits of using international credits for ETS breathing space?

Short term, international credits could deliver a one-off benefit via lower cost. Given durable removals' likely greater capacity and cost efficiency globally, international optionality and efficient siting of carbon removal projects are welcome for the additional cost benefits they could bring, especially long term.

But over the medium to long term, relying on them for European net-zero and net-negative goals locks us into novel, unhelpful and costly dependencies. International credits must thus be used as a complement to the domestic transition, if used at all. International credits used to buffer the ETS also risk raising both European and global emissions if the credits are not compatible with the like-for-like principle.

What is Carbon Gap's policy ask?

Overall, the use of international credits to inform the EU ETS cap is **not a first-best option for policy design**, given the risks outlined above. Nonetheless, where international credits are used, the following policy measures are needed:

- › **Develop an international credits hierarchy.** We suggest a mitigation hierarchy that, after domestic emissions reductions, favours domestic carbon removals over international credits.¹¹
 - We suggest prioritising domestic carbon removals until 2040. This is needed to kickstart a domestic CDR sector, capture the growth and employment benefits of innovative CDR solutions and harness their potential to transition European industry.
 - Any use of international credits must adhere to the like-for-like principle, which requires counterbalancing long-lived fossil emissions with a correspondingly durable mitigation project to fully neutralise their impact. Durable carbon removal projects are therefore a strategic priority for any international credit portfolio, especially when backing ETS breathing space.
 - Lastly, the ETS's existing linkages – with the European Economic Area (EEA) and Swiss systems, and with the UK in future – may already require Article 6 credits to be considered for seamless integration between the countries. Geological carbon storage projects such as the Norwegian Northern Lights or the Icelandic Coda Terminal, both located outside the EU's NDC borders, might be relevant within this scope. These projects may warrant considering international credits from carbon removal projects, e.g. combined with on-site DAC. The EU should provide additional priority to international credits from already linked systems and strive for a fast-paced establishment of regulatory clarity.

¹¹ The hierarchy also applies where ETS revenues finance breathing space for covered entities.

6. WILL THE ETS DELIVER FOR CDR? THE DEVIL IS IN THE DETAIL, AND COMPLEMENTARY POLICIES REMAIN KEY

ETS integration alone will not generate sufficient near-term demand to sustain the project pipeline needed for long-term scale. A public authority will play an impactful role – running competitive auctions can aggregate demand and reduce transaction costs for both buyers and suppliers. However, complementary demand-side policies are essential to bridge the gap between today's voluntary market and a mature regulated one via the ETS. Several mechanisms warrant priority attention: national procurement schemes; public procurement mandates and municipal incentive structures that enable local governments to count CDR purchases toward their climate targets; and regulatory clarification on how permanent CDR contributes to the EU's 2040 climate target and how that contribution will be distributed across Member States, with the November allocation expected to be a defining signal for national policy ambition. Continued support for voluntary private buyers can also bridge the gap, leveraging the EU Buyers' Club and providing guidance on CDR use cases to de-risk corporate claims. Finally, a revision of the ReFuelEU Aviation regulation to allow CDR as a flexibility mechanism for meeting sustainable aviation fuel quotas would open a significant and structurally motivated demand stream from one of the hardest-to-abate sectors in the European economy, though this option remains under active consideration and would require further regulatory assessment before inclusion in formal policy recommendations.

7. CARBON GAP'S CORE ASKS FOR ETS INTEGRATION

We anticipate that a public authority integration with added breathing space will be pursued in the upcoming legislative proposal. Given this, it is critical that the following features should be addressed in any legislative proposal.

Recommendation 1: Integrate via a public authority with a clear mandate. A public authority has several key advantages over an operator/direct integration, namely nurturing a balanced CDR portfolio and creating timely CDR demand at scale. However, it presents added administrative costs, and may expose the Commission to greater risk, which could make it politically less attractive. We hope to see the public authority placed on a firm footing with a clear rationale for its existence, otherwise we risk slipping towards a less strategic approach through co-decision. Once the CDR market has matured, an eventual transition to operator/direct integration could promote greater competition, reduce public support needs, and enable a polluter pays approach.

Recommendation 2: Integrate CDR purchases “below the cap” as much as possible. The options presented on 12 May indicate the Commission is not actively looking at a public authority integration *below* the cap. Yet “above the cap” and “one-in-one-out” are not mutually exclusive approaches. The EU can and should seek to integrate CDR within the existing cap as much as possible in the near term, limiting its use as an added source of “flexibility” in the ETS. Nonetheless, an eventual transition to above-the-cap integration is likely needed to achieve a net-zero ETS.

Recommendation 3: Adopt tools for addressing the price gap. Since the EUA price will only recover part of the cost of CDR units, the EU also needs a clear plan for funding the remainder, and how these costs will be reduced over time. The EU and Member States should direct a gradually increasing share of ETS funding to supporting CDR to address residual emissions, while also building an investable policy framework for CDR through updates to state aid rules and permitting regimes.

Recommendation 4a: Introduce a legal quality threshold for CDR methods. To future-proof for CRCF scope expansion and safeguard against lower-durability CDRs entering the ETS and driving mitigation deterrence, a clear legal benchmark is needed to determine which CDRs are appropriate for the ETS. The benchmark should build on specific monitoring and liability requirements that are aligned with the ETS Directive and CCS Directive.

Recommendation 4b: Target a balanced CDR portfolio. Early procurement rounds should be organised in buckets to ensure a mix of BioCCS and DACCS; if the two methods are forced to compete on price at the early stages, DACCS will struggle to enter the ETS and will not benefit from the demand pull needed to scale projects.

Recommendation 5: Develop an international credits hierarchy. A mitigation hierarchy that, after domestic emissions reductions, favours domestic carbon removals over international credits, is needed to strengthen the domestic industrial transition and kickstart a domestic CDR sector. Any use of international credits for the ETS should follow the like-for-like principle.

Recommendation 6: Long-term market making. The public authority will help promote a more level playing field in the near term while CDR is nascent. But ETS policy should eventually aim to create a competitive market for CDR in the long term, which will in turn reduce the need for public support and uphold polluter pays. For example, the Commission must run CDR procurement to ensure sufficient competitiveness and limit market distortion – namely specifying how it will set appropriate purchase prices. Regular procurement rounds will be needed, rather than a one-off round which will only benefit a small set of suppliers. Procurement should move from structured sourcing across multiple method buckets to a more competitive approach over time. A move towards an operator-led integration, and a switch to above-the-cap, could eventually be helpful in promoting competition.

Recommendation 7: Establish an explicit volume mandate. With the ETS positioned as a central tool for funding EU CDR, the proposal must make explicit the number of tonnes targeted through the ETS. This clarification also enhances accountability and underpins the public authority discussed mandate below.