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ETS Evolution – How can Art. 192 TFEU serve as a legal basis for the reform of the EU Emissions Trading Directive?

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The European Commission (EU Commission) will publish their proposals for the reform of the European Emissions Trading System Directive 2003/87/EC (ETS Directive) in mid-July 2026. The process is mandated by the Emissions Trading System Directive itself: Art. 30 par. 5 ETS Directive requires a report to the European Parliament and Council, "where appropriate accompanied by a legislative proposal and impact assessment" that addresses negative emissions from carbon dioxide removals (CDR), lowering of the 20 MW threshold currently applied for activities covered by the European emissions trading system (EU ETS) and the effective accounting of emissions under the Directive, including such in processes of Carbon Capture and Use (CCU).

However, recent months have brought to light additional issues relating to the proper functioning and the future development of the European emissions trading system, which are expected to the addressed by the EU Commission as well. Such include inter alia measures to postpone the so-called "endgame" of the European emissions trading system, i.e. that de lege lata post 2039 hardly any new emissions allowances could be allocated.

Generally, all EU legislative action needs to be based on a competence given to the EU legislator within the Treaties, and the respective procedures need to be followed; otherwise the legal act can be declared void by the European Court of Justice. In case of the EU Emissions Trading Directive, the legal basis has so far been Art. 192 par. 1 Treaty on the Functioning of the European Union (TFEU). That provision allows legislation which serves the EU's environmental policy objectives under Art. 191 TFEU to be adopted in the course of the ordinary legislative procedure, with majority voting in the European Parliament and the Council. Note that this study does not examine Art. 194 TFEU, the competence in the field of energy policy, as a legal basis for the EU emissions trading system.

The EU Emissions Trading Directive and its amendments to date have thus been adopted with qualified majorities. However, – inter alia – for *"provisions primarily of a fiscal nature"*(lit. a)) and "*measures significantly affecting a Member State's choice between different energy sources and the general structure of its energy supply*" (lit. c)) (abbreviated as a Member State's "energy souvereignty"), Art. 192 par. 2 s. 1 TFEU prescribes the special legislative procedure. Under those procedural rules, the Council votes unanimously, while the European Parliament is only consulted.

Considering the importance of the choice of legal basis for current – and future – reforms of the Emissions Trading Directive, this study examines the scope of the exceptions under Art. 192 par. 2 TFEU. In the context of such reforms, it thus discusses

- What makes a provision be primarily of a fiscal nature (lit. a)); and

- What measures are significantly affecting a Member States' energy souvereignty (lit. c)).

With regard to the former, „*provisions primarily of a fiscal nature*" is not defined in primary EU law. However, based on the common understanding of the terms, as well as the United Airlines decision of the European Court of Justice on the matter (European Court of Justice, judgment of 21.06.2018 – C-5/16 – Poland/European Council and Parliament), one can deduce certain criteria to delineate its meaning. The term "primarily" thereby seems to relate to the general rule that the main focus of a legislative act determines the appropriate legal basis. Accordingly, a provision may be primarily of fiscal nature for the purposes of Art. 192 par. 2 s. 1 lit. a) TFEU where

- It is intended to generate income for general budget of the (EU) legislator; and
- The obligation to pay is not accompanied by any direct benefit in return.

In emissions trading systems like the European emissions trading system, it may also be relevant that the price for the emissions allowances is determined by supply and demand in the market.

The latter exception, i.e. measures significantly affecting a Member State's energy souvereignty under Art. 192 par. 2 s. 1 lit. c) TFEU, is not clearly defined in the TFEU either. Based on the legal interpretation methods including textual interpretation, and the judgment of the European Court of Justice on the market stability reserve (European Court of Justice, judgment of 21.06.2018 – C-5/16 – Poland/European Council and Parliament), it encompasses those measures where

- It follows from "the aim and content (...) that the primary outcome sought by that measure is significantly to affect a Member State's choice between different energy sources and the general structure of the energy supply of that Member State" (European Court of Justice, *ibid* par. 46); and
- Where the effect is not only indirect

Key Findings

- The EU Emissions Trading Directive – and its reforms – have so far been based on Art. 192 par. 1 TFEU; the ordinary legislative procedure has been followed with majority voting in the European Parliament and the Council.
- Reforms that are intended primarily to generate income for the EU general budget and which would take away the consideration in return for the payment obligation would constitute provisions primarily of a fiscal nature under Art. 192 par. 2 s. 1 lit. a) TFEU . They would thus necessitate the special legislative procedure, with unanimous voting in the Council.
- Art. 192 par. 2 s. 1 lit. c) TFEU requires the same special legislative procedure for reforms that are intended to and based on their content significantly restrict a Member State in the choice between different energy sources and the structure of their energy supply, where the effect is not only indirect.