Creating positive impact with ETS2

Using money raised from fossil fuels to support affected households.

LIFE Effect

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Introduction

This brief shows how the new Emissions Trading System (ETS) provides EU countries with sufficient funds to mitigate financial burdens for households. The policy options for member states are presented with a tool to evaluate specific policies. This is an invitation for social and climate experts to engage with the implementation of carbon pricing in buildings and transport (ETS2).

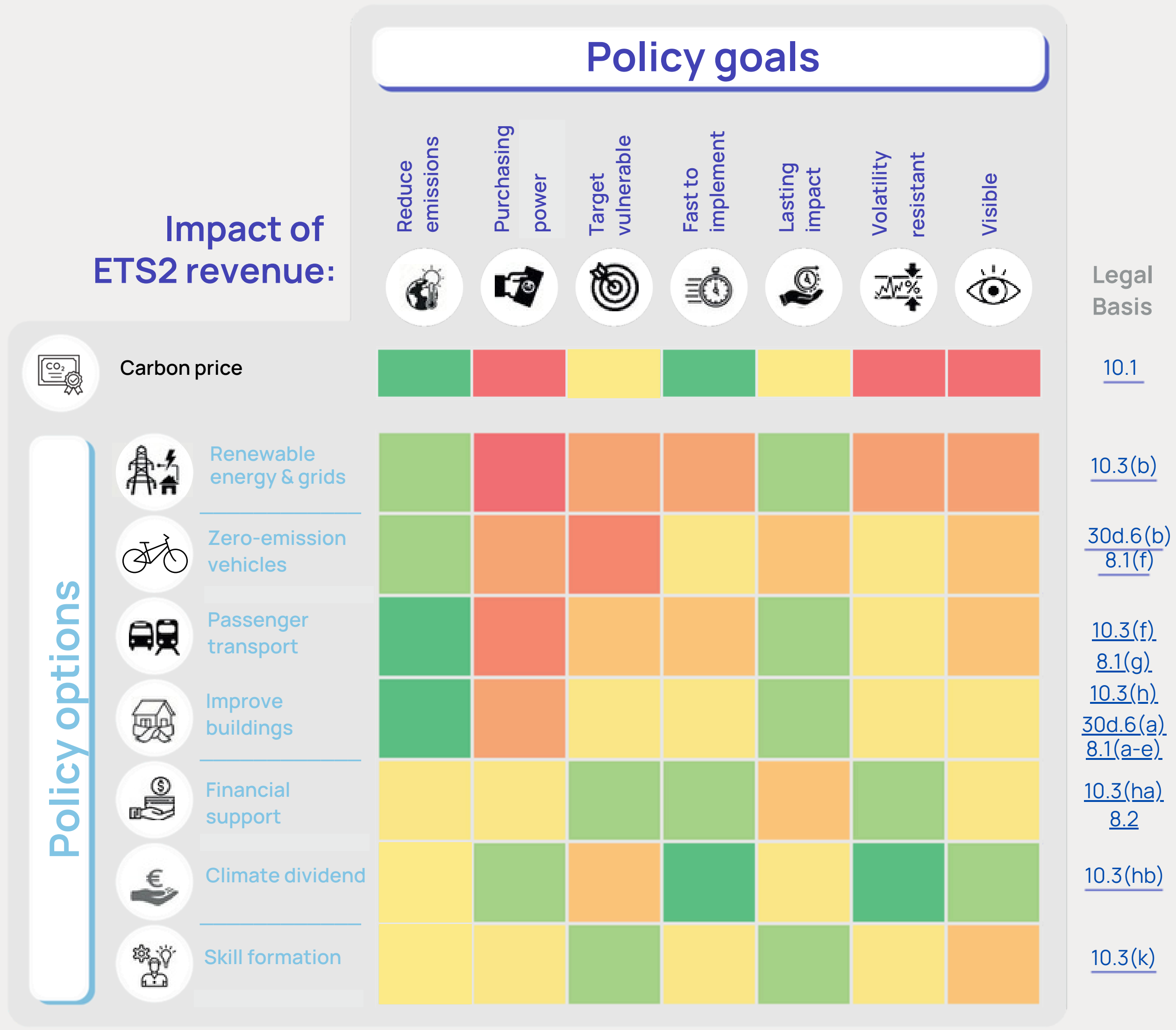
Framework

Carbon pricing under ETS2 will raise prices of fossil fuels in heating and transport and thus of all products which include these as inputs. EU countries are therefore required to use the revenues "giving priority to activities that can contribute to addressing social aspects of the emissions trading".

The revenues produced from ETS2 go far beyond the scope of the Social Climate Fund (SCF), which is intended to specifically support those most vulnerable to price increases from emissions trading. If the early market signals are an indication of the order of magnitude of ETS2 prices (around €75 per ton of CO2), this would generate €344.48 billion in revenue that can be used to support households in the transition and fund the switch to decarbonised technologies. It would also be possible to use revenues from ETS1 (carbon pricing in industry) to help households adapt to higher prices.

The ETS legislation only allows a limited number of activities to be funded directly from ETS revenues. Of those, only a few address the social impact of emissions trading. These are listed in the table below, where the policy revenue options are cross-tabulated with the policy goals. Each **Policy Option** and **Policy Goal** is outlined and colour-coded below. In the column **Legal Basis** in the table you find links to relevant paragraphs in three articles that are relevant for ETS2 revenue use:

- Article 8 from the SCF Directive describes the use of SCF funds to support vulnerable households and micro-enterprises.
- Article 30 from the ETS Directive is specifically about addressing the social impact on all households.
- Article 10 from the ETS Directive prescribes the use of all ETS revenue, including ETS2.



Articles refers to relevant paragraphs of EU legislation governing ETS2 revenue use:
Article 8 of the SCF Directive that describes the use of SCF funds to support vulnerable households and micro-enterprises. Article 30 from the ETS Directive that is specifically about addressing the social impact on all households. Article 10 from the ETS Directive that prescribes the use of all ETS revenue including ETS2. The colours in the cells are indicative of the strengths and weaknesses of each option in terms of each goal — detailed explanation in the text.

1 Policy Options

We distinguish four types of measures that can be funded from ETS2 revenues.

Some measures aim to develop technologies and infrastructure to replace fossil fuels and to reduce emissions by investing in renewable energy and electricity grids. These investments are required for the energy transition, but the effect on households' income is not always direct and vulnerable households are hard to reach.

Positive examples that can deliver strong direct effects include energy communities specifically for low-income households or other profit-sharing energy models.

Then there are measures that directly help citizens transition away from fossil fuels: investments in climate-friendly passenger transport, providing access to zero-emission vehicles, and measures intended to improve buildings through insulation and electrification of heating.

For instance, recent research commissioned by the EEB shows that investing 34% of the SCF and other ETS2 revenues would be enough to decarbonise the heating and cooling of almost all vulnerable homes in 23 EU countries and would allow the EU to surpass its 2030 renewable energy target for heating and cooling.

The funds can also be used to provide income support to households to compensate for higher prices and stimulate household investments in emissions reduction.

Targeted financial support can help address energy poverty. National climate dividend schemes cover large parts of the population and can increase public support.

The revenues can also be used to promote skill formation to contribute to a just transition. The transition will make old jobs in the fossil fuel industry obsolete whilst creating new opportunities in decarbonised sectors and industries. Skills development programmes can be targeted to vulnerable groups via the SCF.

2 Policy Goals

We identify seven policy goals that can be achieved with these different revenue uses.

The overarching goal of carbon pricing is to **reduce emissions**. This is primarily achieved by pricing emissions, but it can also be stimulated by revenue use.

Higher fuel prices have a considerable effect on households. To **preserve purchasing power**, policy-makers can reduce dependence on fossil fuels, reduce other taxes, or implement measures that increase household incomes.

The SCF requires countries' spending plans to **target vulnerable households**. Carbon pricing itself is highly targeted as it depends on fuel consumption, which is higher for high-income households. Investment subsidies often require citizens to co-invest and thereby only reach richer people rather than vulnerable households. Differentiating the amount of subsidies, as well as the eligibility by social criteria, is advisable to counter that effect. Using financial tools to specifically reduce upfront costs (such as leasing models for electric vehicles or heat pumps) has shown to be particularly impactful.

As the pricing takes effect in 2027, social support must also be **fast to implement**. Means-testing is often administratively and politically difficult and targeting investments on vulnerable groups is even more challenging. Countries that have a well-functioning social security infrastructure can provide socially targeted payments more efficiently.

The SCF legislation separates measures with **lasting impact** from direct income support. However, direct payments can also make a lasting impact if they are used for investments in decarbonised technologies, such as paying off a loan for home improvements.

The ETS2 price may fluctuate. Social measures need to be **volatility resistant** and shield consumers from the extra risk.

ETS2 results in a visible price increase at the gas station that will create opposition. For continued political support, the use of the revenues should also be **visible** and comprehensible so that it can be well communicated.

Policy Evaluation

We have listed the Policy options in a matrix, rating how they score on the listed **Policy goals**. This allows for comparison of policy proposals on how they impact the different goals. Scores are indicative, as different measures in the same category could score differently. For example, in the category Passenger transport a subsidy on tickets for a high-speed train between European finance centres would score differently to a new commuter tram service in a mining area, although they both concern passenger transport. The actual score depends on the specific measure in the listed category and the context, which will be elaborated on in country-specific applications of this tool.

The above table highlights that there are significant trade-offs. For example: between targeting vulnerable households and protecting households' purchasing power; or seeking a lasting impact and offering fast relief to households. A successful mix of revenue uses will account for the most pressing needs in specific EU countries, allow for sequencing of policies over time, include an insurance mechanism for high prices, and provide a framework for comparing and evaluating the revenue uses.

Next Steps

The National Social Climate Plans prepared in the first half of 2025 offer a first opportunity to discuss the use of revenues from ETS2.

To support the successful implementation of ETS2 we need social and climate policy experts to work together on effective revenue use. Through the impact of revenue disbursement, ETS2 has the potential to combine climate policy with a positive social impact in the EU. The importance of social priorities has not yet been internalised by all EU governments. This is exemplified by the fact that the climate ministries, not social ministries, are responsible for the SCF and ETS2 revenue use in nearly all EU countries.