

Brussels, 09.12.2025

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ETS EVOLUTION

ASSESSING THE LEGAL FRAMEWORK FOR A(NY) REFORM OF THE EU ETS DIRECTIVE



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AGENDA

- › Choosing the right legal basis for reform
- › The EU ETS as „provisions primarily of a fiscal nature“ (Art. 192(2) subpar. 1 lit a) TFEU)?
- › Does the EU ETS significantly affect a Member State’s energy sovereignty (Art. 192(2) subpar. 1 lit. c) TFEU)?

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CHOSING THE RIGHT LEGAL BASIS FOR REFORM

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ECJ ON THE CHOICE OF LEGAL BASIS (I/II)

›“the choice of the legal basis for an EU measure must rest on **objective factors amenable to judicial review**, which include, inter alia, the **aim and content of that measure**” (Eg. Case C-36/98 Spain v Council, par. 58f; Case 5/16 Poland v Parliament and Council, par. 38)

›What counts for the **choice of legal basis** are **aim and content of the reform**.

›“Given that, in order to know the real and specific effects of a legislative measure, it is necessary to analyse those **effects after its entry into force**, the legislature’s choice would have to be **based on assumptions as to the likely impact of that measure**, which, by their nature, are speculative and are in **no way objective factors amenable to judicial review** within the meaning of paragraph 38 above.” (Case 5/16 Poland v Parliament and Council, par. 41)

›**Effects (after entry into form)** are **not factors** to be considered in choice of legal basis.

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ECJ ON THE CHOICE OF LEGAL BASIS (II/II)

“If examination of a Community measure reveals that it pursues a twofold purpose or that it has a twofold component and if one of these is identifiable as the main or predominant purpose or component whereas the other is merely incidental, the act must be **based on a single legal basis**, namely that required by the main or predominant purpose or component”. (E.g. Case C-338/01 European Commission v Council, par. 55)

› Normally **single legal basis based on main or predominant aim and content of reform.**

› **Dual legal basis** only in **exceptional circumstances**, provided that the legislative procedures required can be reconciled (E.g. Case C-338/01 European Commission v Council, par. 56ff)

And why are we talking about this?

› The ECJ can declare void acts not based on the correct legal basis/adopted according to the wrong procedure

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LEGAL BASIS OF THE ETS DIRECTIVE

Current legal basis: **Art. 192(1) TFEU** = competence to legislate in order to pursue the **Union's environmental policy**

› Procedure to be followed: „**ordinary legislative procedure**“ with qualified majority voting in the Council and the Parliament

HOWEVER: **Art. 192(2) subpar. 1 TFEU** covers „**provisions primarily of a fiscal nature** (Art. 192(2) subpar. 1 lit. a) TFEU) and „**measures significantly affecting a Member State's choice between different energy sources and the general structure of its energy supply**“ (Art. 192(2) subpar 1 lit. c) TFEU)

› Procedure to be followed: “special legislative procedure” with unanimity in the Council and the Parliament only being consulted

In theory: **Art. 192(2) subpar. 2 TFEU** provides a “**bridge**”

› **Council can decide unanimously that ordinary legislative procedure shall apply**

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**DOES THAT MEAN THAT A(NY) REFORM OF THE EU ETS
DIRECTIVE CAN STILL BE BASED ON ART. 192(1) TFEU?**

Let's investigate.

THE EU ETS AS „PROVISIONS PRIMARILY OF A FISCAL NATURE“ (ART. 192(2) SUBPAR. 1 LIT A) TFEU)?

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ECJ ON EU ETS (CASE C-388/10 UNITED AIRLINES)

›ETS is climate protection measure

›**Aim and content are climate protection**, thus implying that Art. 192 is the right legal basis (par. 139)

›Emissions trading systems are different from „obligatory levies“

›**Issuance of (limited number of allowances) creates incentive** for obligated parties to reduce GHG emissions; trade in allowances can even lead to profits (par. 141f)

›ETS “**is not intended to generate revenue for the public authorities**” (par. 143)

›NOTE: the ECJ had been asked in this case whether the ETS (or its extension to a aviation) would constitute a CONSUMPTION TAX, so many of the considerations are specific to that question

›And ECJ suggests that within ETS there is no direct link between the price to be paid and the amount of fuel consumed

›**But no one (nowadays) really claims the ETS to be a consumption tax, right?**

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(LEGAL) LITERATURE ON PROVISIONS PRIMARILY OF FISCAL NATURE

„Tax“ not defined in primary EU law

- › However, term used in several legal acts and discussed in case-law
- › Normally understood as measures
 - › That **generate income for the (state) budget;**
 - › And that are not **followed by an individual return.**

In the economics literature, emissions trading systems also referred to as „quantity-based“ measures, as the **cap on emissions allowances (supply and demand; thus: the market) determines the price**

- › As opposed to „price-based“ measures, with the price being set by regulation

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SUMMARY: CRITERIA TO DEFINE „PROVISIONS PRIMARILY OF A FISCAL NATURE“ (ART. 192(2) SUBPAR. 1 LIT. A) TFEU)

The measure is likely a provision primarily of fiscal nature, if it

- ›Generates **revenue for the (EU) budget**;
- ›Is not followed by an **individual return**; and/or
- ›**The price to be paid is fixed** by the regulator.

Note: not clear from the case-law whether all of those criteria need to be fulfilled (cumulatively) or whether one (or two) are sufficient.

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DOES THE EU ETS SIGNIFICANTLY AFFECT A MEMBER STATE'S ENERGY SOVEREIGNTY (ART. 192(2) SUBPAR. 1 LIT. C) TFEU)?

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ECJ ON MARKET STABILITY RESERVE (CASE C-5/16 POLAND V PARLIAMENT AND COUNCIL)

MSR was adopted to remedy structural imbalances in ETS and make it more resistant for future events (par. 60)

› Implying that aim and content are thus – as with ETS – **climate protection** and Art. 192 is the correct legal basis

NOT the aim and content of the MSR significantly to affect Member States' energy sovereignty

› Measures adopted in order to protect the environment and fight climate change „necessarily affect the energy sector of Member States” (par. 44)

› If this would always trigger Art. 192(2) subpar. 1 lit c) TFEU and the special legislative procedure, this would no longer be the exception it is intended to be, but the rule.

› Thus: „higher threshold“ of „significance“ for climate protection measures?

Also: MSR (and ETS) are technology neutral (par. 64), so effects on energy sovereignty are **only indirect** (par. 68)

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SUMMARY: CRITERIA TO DEFINE „MEASURES SIGNIFICANTLY AFFECTING A MEMBER STATE’S ENERGY SOUVEREIGNTY“ (ART. 192(2) SUBPAR. 1 LIT. C) TFEU)

The measure is significantly affecting a Member State’s energy sovereignty, if

- › **Its aim and content are to restrict** a Member State’s choice between different energy sources and the general structure of its energy supply; and
- › **The effects are not only indirect.**

Note: in the field of climate protection, the ECJ seems to see a higher threshold for what constitutes „significant“.

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AND WHAT DOES THAT MEAN FOR THE EVOLUTION OF THE ETS?

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HAS THE ETS DIRECTIVE ALREADY BECOME A MEASURE THAT SHOULD HAVE BEEN BASED ON ART. 192(2) TFEU (RATHER THAN ART. 192(1) TFEU)?

›For example...

›Because of the ETS „endgame“ itself?

›Because of the introduction of the Market Stability Reserve?

›Because of the target price in the ETS 2?

›...

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WILL REFORMS OF THE ETS DIRECTIVE TRIGGER ART. 192(2) TFEU?

›For example...

›EU COM proposal to raise own resources from the EU ETS?

›Reforms of the market stability reserve?

›Inclusion of flexibility/CDR (within EU, outside EU)?

›Delayed phase-out of free allocation?

›...

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THANK YOU FOR YOUR ATTENTION

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