

EU ETS Reform Must Safeguard Industrial Competitiveness and Enable Transformation

BASF Position on the European Commission Proposal for the Revision of the EU Emissions Trading System

The Commission proposal fails to deliver the fundamental change of course needed to safeguard Europe's industrial base and enable transformation. The EU chemical industry is in a position to compete successfully in the global marketplace, provided there is a global level playing field making this possible. Today, the sector is facing weak demand, high energy costs, import pressure and, consequently, declining investment. In the current situation, the ETS must not further increase unilateral burdens and ignore both the competitiveness of existing assets and the realities companies are facing to create viable business cases to transform. Priority of the ETS reform must be to preserve effective carbon leakage protection, establish realistic benchmarks and create viable conditions for transformation investments in Europe, in particular instruments to create market demand for low- carbon products.

Unfortunately, the proposal's limited improvements are more than offset by measures that further increase unilateral cost exposure and investment uncertainty. Moreover, the impact of these improvements largely comes too late, while conditional free allocation and the unchanged benchmark logic imply sharply increasing costs from 2031. Transformation cannot be mandated where scalable and mature technologies, competitive low-carbon energy and feedstocks, infrastructure, financing, customer demand and willingness to pay are missing in a globally competitive environment.

Transformation of chemical manufacturing in the EU comes with high costs for CAPEX and permanently higher OPEX that are not faced by competitors in other regions. Without mechanisms to compensate for these permanent structural cost disadvantages for globally exposed industries, manufacturers are unable to develop viable business cases for transformation. Conditions to force companies to either spend massively in ETS costs or go for unfeasible transformation routes will reduce manufacturers' competitiveness and trigger further closures of upstream assets with serious consequences for entire value chains.

Instead of accelerating the decline of energy-intensive manufacturing, the ETS reform needs to be part of a policy-mix that provides effective carbon leakage protection and the enabling conditions necessary to create viable business cases for industrial transformation.

BASF calls on the European Parliament and Member States to:

Preserve free allocation as an effective carbon leakage safeguard

Free allocation compensates only part of the unilateral carbon cost borne by EU producers and therefore is not an investment subsidy. The ETS revision further widens the unilateral cost gap between EU producers and global competitors. As long as producers outside the EU do not face equivalent carbon costs, free allocation remains indispensable to limiting carbon leakage and maintaining investment capacity in Europe. Reducing free allocation without an effective alternative safeguard weakens European production, accelerates the shift of investments and emissions abroad and ultimately jeopardizes the resilience of Europe and its industrial value chains.

While decarbonisation measures have been identified, conditionality is not creating viable business cases. The proposed conditionality link between 80% of allocation to a decarbonisation plan and the ex-post release of the remaining 20% against investments and emission-reduction milestones goes against investment budgets and increases cost exposure, financing needs, bureaucracy and legal uncertainty. Implementation of decarbonisation measures is further constrained by insufficient infrastructure, including CO₂ and hydrogen pipelines, and the limited maturity of key technologies. Companies could thus lose free allocation even where implementation depends on factors beyond their control. For the most vulnerable value chains, the resulting full ETS cost exposure could force decisions on the viability or closure of European assets as early as 2031. It could also force non-economic investments, further deteriorate competitiveness and reduce companies' capacity to finance transformation.

For CBAM products, the planned phase-out of free allocation already reduces its economic value and jeopardizes the chemical downstream value chains through unilaterally increased cost burden. Moreover, additional conditionality doesn't apply to imports into the EU, giving them a competitive advantage over domestic production. CBAM sectors should therefore be exempt from the proposed conditionality - though respective decarbonisation investments should be counted under the proposed pooling mechanism as these contribute to the decarbonization of the downstream chemical value chains. Furthermore, ammonia for industrial value chains must be excluded from CBAM, as - contrarily to ammonia's fertilizer downstream products - the multitude of industrial downstream derivatives of ammonia can't effectively be protected under CBAM. Decarbonisation plans should support strategic planning rather than serve as a mechanism for withholding carbon leakage protection. Requirements must recognise integrated sites, avoid duplication and provide flexibility where enabling conditions are absent. Given its far-reaching consequences, the proposed conditionality concept should first be critically assessed and discussed in depth with the sectors concerned. Only on this basis should a political decision be taken on whether and how to pursue the approach.

Create conditions to make transformation in the EU viable

The EU Commission's intention to provide more budget for transformation via the Industrial Decarbonization Bank or the Investment Booster program can only support a very limited number of projects, given the massive funding gap in chemical upstream assets because of high CAPEX requirements and persistently higher OPEX costs in the EU compared to global markets. For globally exposed products in particular, transformation will only be a viable alternative to closure if funding schemes fully cover the resulting competitiveness gap. While those programs can serve as a temporary piece in the policy mix, it is a pre-requisite that the EU and its Member States prioritize developing a policy framework, which permanently:

- reduces carbon abatement costs by co-financing and de-risking H₂ and CO₂ infrastructure costs (H₂/CO₂ grids, CO₂ sinks),
- reduces costs for green electricity and low-carbon hydrogen by reducing taxes, levies and fees and designing feasible and technology-neutral certification rules,
- allows cost pass-through of transformation costs to end-consumers via horizontal market-pull policies such as the European Chemicals Resilience Initiative (ECRI) to create permanent and reliable revenue streams to transforming manufacturers upstream,
- reflects the needs of publicly listed companies for predictable, bankable, technology-neutral and feasible conditions to plan and execute complex chemical transformation projects.

Fundamentally reform product and fallback benchmarks

Benchmark values must remain representative of what is technologically and economically achievable across the sector. Non-representative and overly stringent benchmarks further reduce free allocation and increase ETS cost exposure for chemical value chains beyond feasible levels. The best-10% methodology should therefore distinguish broadly reproducible performance improvements from exceptional site conditions, subsidised pilot projects and non-

scalable configurations that cannot realistically be replicated across the industry. Installations benefiting from unique infrastructure, favourable energy access, exceptional product portfolios or substantial public support must not set unrealistic standards as they could otherwise disproportionately tighten benchmarks for installations unable to replicate those conditions.

Where the performance of the top 10% deviates significantly from the sector median, the resulting benchmark no longer represents a technically and economically achievable performance level. In such cases, benchmark progress should be assessed against improvements in the median rather than the top 10%. More representative benchmark values can only provide effective carbon leakage protection if they are accompanied by sufficient free allocation volumes and are not neutralised by the cross-sectoral correction factor.

The minimum reduction rate should be removed, and a legal safety net should allow benchmarks to be frozen or limited where enabling conditions are absent. Heat benchmarks should be differentiated by application, temperature level and technology, rather than by formal sector categories alone. Their design should reflect the different decarbonisation options and technical and economic constraints of low-, medium- and high-temperature applications. Methodological corrections should be introduced as early as possible and not be postponed to the post-2030 period.

Deliver earlier relief and long-term predictability for the cap trajectory

BASF welcomes the lower Linear Reduction Factor proposed from 2031 and the recognition of residual industrial emissions. However, the aggressive cost trajectory before 2031 remains unchanged, while the post-2036 path depends on a later assessment of international credits. A lower LRF, or an equivalent cap and allowance correction, should apply before 2031, and the long-term trajectory must be fixed early enough to support industrial investment decisions.

Restore market liquidity and cost-efficient flexibility

BASF supports reforming the Market Stability Reserve to reduce artificial scarcity and stopping allowance invalidation. High-quality Article 6 credits and certified permanent removals should become usable significantly earlier and be directly accessible to compliance entities, instead of being limited to centrally managed purchasing mechanisms. Eligibility should build on the Paris Agreement and the EU Carbon Removal Certification Framework without unnecessary EU gold-plating, and the framework should remain technology-open while safeguarding environmental integrity.

Recycle ETS revenues into industrial competitiveness and transformation

A substantial and binding share of EU and national auction revenues should support ETS sectors through competitive low-carbon energy, electricity, hydrogen and CO₂ infrastructure, indirect cost compensation, de-risking of transformative investments and demand-side measures. Revenues must not disappear into general budgets, and ETS-based funding should complement, not replace, additional public and private financing.

Industrial transformation requires a globally competitive industrial base. The EU ETS can contribute to climate neutrality only if companies remain able to invest and produce in Europe. Low-carbon production in Europe will remain structurally more expensive than conventional production and competing imports. Therefore, permanent mechanisms are needed to compensate these additional costs and maintain viable business cases for industrial transformation.

Funding, enabling conditions, carbon leakage protection and carbon pricing must therefore work as one coherent framework. The sequence matters: transformation follows enabling conditions. Tightening benchmarks or withholding free allocation cannot substitute for infrastructure, competitive energy and feedstocks, bankable technologies, financing and markets for low-carbon products. **The co-legislators should correct the proposal accordingly and provide early legal certainty before key design choices are transferred to delegated acts.**