Going Beyond the Omnibus:

How the EU's Climate Policy Can Be Simplified

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Summary

- The paper argues that EU climate policy has become overly complex and costly, undermining competitiveness without delivering additional emissions reductions. It calls for simplification centred on cost-effectiveness rather than layered regulation.

- Its core finding is that a single, comprehensive emissions pricing system is the most efficient way to reduce greenhouse gas emissions. Uniform carbon pricing ensures that emissions are cut where it is cheapest to do so across the economy.

- The EU Emissions Trading System (ETS) already provides a strong foundation for cost-effective climate policy, especially once ETS2 is implemented. However, overlapping rules such as the Effort Sharing Regulation (ESR) create double regulation that raises costs without lowering total emissions.

- Sector-specific targets and bans, including those on internal combustion engines, renewable energy quotas, and energy efficiency mandates, are shown to undermine cost-effectiveness. Under a binding ETS cap, these measures shift emissions rather than reduce them, while increasing the cost of the transition.

- The paper recommends merging ETS and ETS2 into a single system and extending coverage to all sectors, including agriculture. This would ensure a uniform carbon price across the entire EU economy.

- It further recommends abolishing overlapping member state obligations under the ESR and scrapping sector-specific climate regulations altogether. Removing these would simplify policy, lower costs, and improve EU competitiveness.

About the author

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The ideal EU climate policy entails uniform pricing of emissions

To understand what an ideal EU climate policy would look like, it is helpful to consider the economic principles that guide responses to issues such as climate change. The emission of GHGs into the atmosphere causes global temperatures to rise, adversely impacting production, the environment, and public health. As the actions of one emitter negatively affect others globally, GHG emissions are defined as a negative externality. Basic economic theory suggests that externalities are most efficiently addressed through pricing. One approach is to levy a Pigouvian tax on the activity generating the negative externality (Pigou 1920). Another is to implement cap-and-trade schemes for GHG emissions. Both approaches internalise the cost of GHG emissions in production, ensuring that production takes place only when the benefits exceed the cost of emissions.

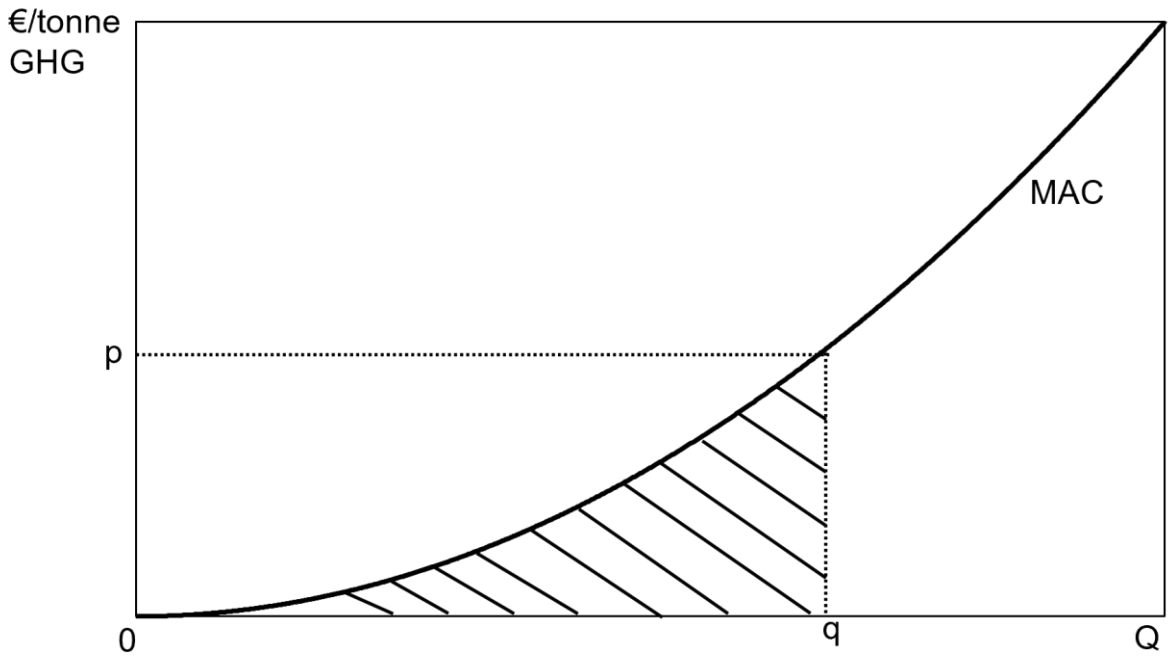
Ideally, GHG emissions should be priced according to their global marginal damage cost, as this would maximise global economic welfare. However, it is difficult to determine that price precisely. Some estimates suggest that it lies in the range of €60–150 per tonne of CO_2e (carbon dioxide equivalent)[1] (Barrage and Nordhaus 2024). A Pigouvian tax is the most relevant instrument for pricing GHG emissions based on their global marginal damage. However, the EU does not have the competence to impose an EU-wide tax.[2] Additionally, the Paris Agreement requires Parties to submit Nationally Determined Contributions (NDCs) that 'contain information on targets, and policies and measures for reducing national emissions...' (United Nations Climate Change, n.d.). The EU participates in the Paris Agreement on behalf of its member states. Together, these factors imply that climate targets and cap-and-trade schemes are the most relevant path for climate policy in the EU, even if this is not cost-benefit optimal.

Nonetheless, it is well established in economic sciences that setting a uniform price for GHG emissions is the most cost-effective way to abate emissions (Mankiw 2009; Tirole 2017). As described previously, this can be achieved through a cap-and-trade scheme. Figure 1 illustrates why a uniform price for GHG emissions ensures cost-effectiveness.

[1] 2024 prices for emissions in 2025.

[2] This is not a call for change; there are other relevant reasons why the EU does not have this competence.

Figure 1. Marginal abatement cost (MAC) curve



Source: Author's illustration

Figure 1 illustrates the MAC curve, which represents the cost of reducing one tonne of GHG emissions. The increasing marginal cost of GHG abatement shows that emissions are relatively inexpensive to reduce initially, for example, through increased energy efficiency. As cheap abatement options are exhausted, abatement costs increase. Further reduction may require the use of more expensive technologies, such as carbon capture and storage (CCS).

Imposing a carbon price, *p*, would enable abatement up to level *q*. In the shaded area, it is cheaper to abate GHG emissions than to pay the carbon price, *p*. Similarly, in the area to the right of *q*, abatement costs exceed the carbon price, so those emissions remain unabated. This ensures that only the most cost-effective abatement measures are implemented and that no abatement effort costs more than the carbon price itself. In an optimal scenario, the carbon price would equal the global marginal damage cost, ensuring that the abatement cost does not exceed its benefits. However, even in a system with emission-reduction targets rather than marginal-damage-based emission prices, carbon pricing still ensures that abatement costs do not exceed the politically determined price.

A uniform carbon price, therefore, ensures cost-effectiveness, which is essential for minimising the cost of the green transition. When mitigation efforts deviate from the most cost-effective path, fewer resources remain for other economic activities. Given the EU's wide range of challenges and goals, it is crucial that cost-effectiveness remains a central goal of the green transition and other areas. The EU should therefore focus on cost-effective climate policies based on uniform pricing of GHG emissions. Compared to current policies, minimising the cost of the green transition will support competitiveness within the EU.

The EU has the core framework in place to achieve its net-zero target cost-effectively by 2050

The EU's main climate target is to achieve net-zero emissions by 2050. In the shorter term, it aims to reduce emissions by at least 55% below 1990 levels by 2030 (European Commission, n.d.). Additionally, the Commission has proposed a 90% reduction by 2040 (European Commission, n.d.). To meet these targets, the EU has adopted several provisions. Emissions in the EU are directly regulated by two classes of regulations, as presented in Table 1.

Table 1. Climate regulations in the EU

	EU-covered emissions		Member state obligations	
Regulation	**ETS**	**ETS2***	**ESR**	**Regulation on land use, land-use change, and forestry (LULUCF)**
Sectors covered	Electricity and heat generation, energy-intensive industries, aviation within the European Economic Area (EEA), and maritime transport.	Buildings, road transport, and additional sectors.	Domestic transport (excluding aviation), buildings, agriculture, small industries, and waste.	Member states are required to ensure that emissions from the land-use and forestry sectors are compensated through the equivalent removal of CO_2.

*Note: ETS2 is scheduled to be fully operational in 2027. However, both EU Member States and the European Parliament have proposed a postponement of ETS2 by 1 year to 2028 (European Commission, n.d.).

Sources: European Commission, n.d., n.d., n.d., n.d.

One class of regulations covers emissions subject to EU carbon trading systems. This class includes the two emissions trading systems – ETS and ETS2. The ETS mechanism is based on the cap-and-trade principle. A cap is set on the total GHG emissions that can be emitted by covered sectors. The EU issues tradable allowances equivalent to the permissible amount of emissions. Companies in the covered sectors must surrender an emissions allowance for each tonne of CO_2e emitted. Companies that emit more than their allocated allowances will have to buy more through the carbon market. Over time, the EU lowers this cap, reducing the number of allowances available and thus increasing the carbon price and incentivising companies to adopt lower-emission practices (European Commission, n.d.). These mechanisms ensure a technology-neutral, uniform price for the covered sectors in the ETS and the ETS2, respectively. Overall, the ETS framework is consistent with a cost-effective, market-based approach to a green transition. When the ETS2 is introduced, almost 80% of the EU's net GHG emissions will be covered by an ETS (Klimarådet 2025). Thus, the ETSs provide a robust foundation for a cost-effective climate policy in the EU.

Another class of EU emissions regulations involves obligations for member states. Initially adopted in 2018, the ESR requires member states to reduce emissions by the covered sectors by 2030. It is worth noting that when the ETS2 enters into force, emissions from buildings and road transport will be covered by both the ETS2 and ESR. This represents costly double regulation, as will become apparent further on.

The LULUCF regulation requires member states to ensure that emissions from the land-use and forestry sectors are compensated through an equivalent removal of CO_2 in 2021–2030.

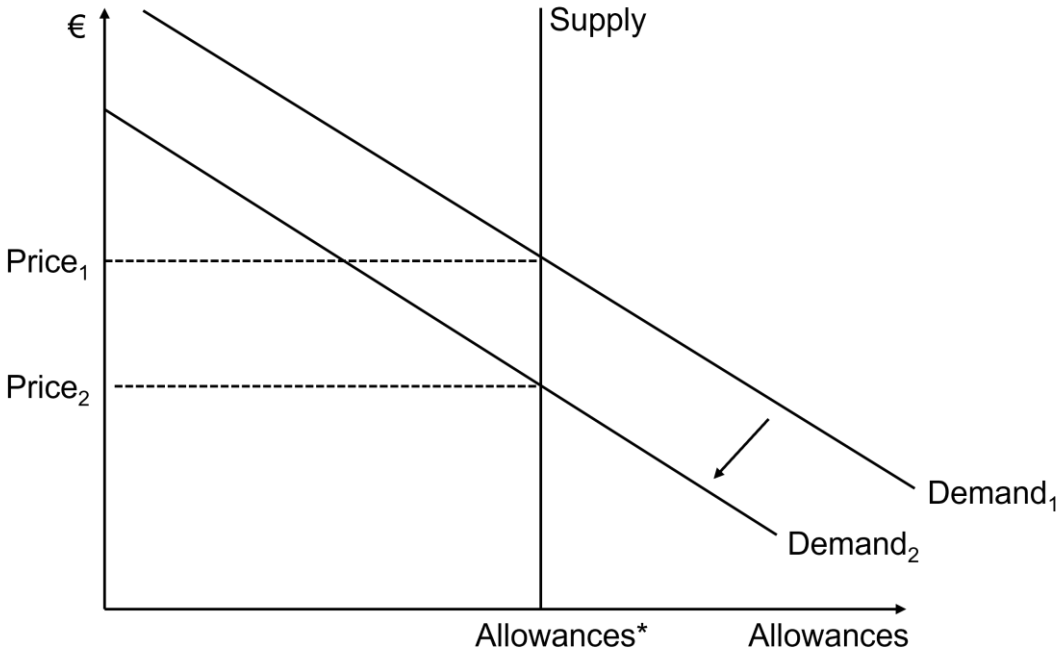
These obligations for member states supplement the ETS regulation, but they will become less relevant once the ETS2 comes into force.

Sector-specific targets undermine the cost-effectiveness of EU climate policy

If the EU were to impose only the regulations listed in Table 1, its overall climate policy would be close to cost-effective. However, in addition to these, EU climate policy includes several sector-specific regulations. These include a ban on new internal combustion engines (ICEs) from 2035. Until then, emissions from newly registered cars and vans must be gradually reduced (European Commission, n.d.). Another sector-specific target requires member states to increase energy efficiency by reducing their energy consumption by 2030 (European Commission, n.d.). Additionally, the EU has a binding renewable energy target: renewable energy must account for at least 42.5% of total energy use, ideally 45%, by 2030 (European Commission, n.d.). Furthermore, suppliers of aircraft fuel must gradually increase the share of sustainable aviation fuels (such as synthetic fuels or advanced biofuels) blended with conventional aviation fuel (European Commission, n.d.). These examples are not an exhaustive list of sector-specific regulations in the EU.

Although sector-specific targets appear to support the goal of achieving net-zero emissions by 2050, they actually undermine the cost-effectiveness of climate policies and are unlikely to have a significant impact on emissions and thus the climate. This is because of how ETSs work, as illustrated in Figure 2.

Figure 2. The number of emissions allowances in an ETS is unaffected by shifts in demand[3]



Source: Author's illustration

[3] The figure is purely illustrative. There are exceptions to this mechanism; e.g., the market stability reserve.

As previously described, an ETS operates on a cap-and-trade principle. Figure 2 shows that the number of allowances (and, consequently, emissions) is determined by the (fixed) supply of allowances (i.e., the cap), while the price of allowances is determined by the balance between supply and demand. If emissions are reduced in a particular sector, demand decreases from Demand1 to Demand2. The price falls, but the number of allowances, and therefore, the total emissions, remains unchanged. The price reduction makes it cheaper to emit GHGs in other sectors covered by the ETS. This mechanism is strongest in a fully efficient ETS, where the carbon leakage rate is 100%. Box 1 describes the mechanisms that affect supply in an ETS. However, these mechanisms do not affect the conclusions on cost-effectiveness, as the ETS is expected to be fully efficient from the early 2030s (Silbye and Sørensen 2023).

Sector-specific targets aimed at reducing GHG emissions, such as the ban on new ICEs, will reduce the demand for allowances. As Figure 2 illustrates, such a shift in demand will not affect total emissions. However, if the ban on new ICEs accelerates the phase-out of ICEs, the cost of the transition will be higher than if this occurred under the ETS. Sector-specific targets, therefore, increase the cost of the green transition and are unlikely to reduce total GHG emissions. As a result, they counteract the cost-effectiveness of EU climate policy.

Box 1. Mechanisms that affect supply in an ETS

The Market Stability Reserve (MSR) may result in leakage rates that differ from 100%. The MSR cancels allowances if there is a large surplus in the market and releases additional allowances if the total number falls below a certain threshold. This implies that the ETS is not always fully efficient. For a more detailed explanation, please refer to Brøns-Petersen and Andersen (2025). The ETS is expected to be fully efficient from the beginning of the 2030s (Silbye and Sørensen 2023), and the mechanism described in Figure 2 is thus expected to apply thereafter.

The fact that the leakage rate can differ from 100% due to the MSR does not constitute an argument either for sector-specific targets or against the ETS. The ETS remains the most suitable form of climate regulation in the EU. Instead, the MSR should be scrapped to allow the ETS to function more cost-efficiently.

In the ETS2, a price stability mechanism is activated if the carbon price exceeds €45 (European Commission, n.d.). The mechanism triggers the sale of additional allowances to keep the price down. Likewise, if the price of allowances rises too rapidly, additional allowances can be released. This soft price ceiling can provide insurance against uncertainty. However, if the mechanism gets activated, climate targets should be adjusted accordingly; otherwise, more expensive abatement measures will be required in other sectors. For an elaborated discussion, please refer to Brøns-Petersen and Andersen (2025).

The changes needed to make EU climate policy more cost-effective

As outlined, the EU already has a framework in place to achieve net zero by 2050 in a cost-effective manner. However, reform of the EU's existing climate policy will be required. Table 2 highlights the necessary changes.

Table 2. Achieving a cost-effective path to net zero in the EU

Changes to the EU climate policy	Why?
Remove member state obligations under the ESR for sectors that are also covered by the ETS2.	Double regulation is costly and is unlikely to have any significant impact on the climate. For this reason, it should be abolished.
Merge the ETS and the ETS2 to create a single ETS.	A single ETS would ensure a uniform price for GHG emissions. Non-uniform prices increase the cost of the green transition, as cheaper reductions would be available at a lower price.
Include all EU emissions in a single ETS, including those from agriculture.	This would ensure uniform pricing of all GHG emissions, which is necessary for cost-effectiveness.
Abolish all sector-specific climate targets and regulations.	Sector-specific targets and regulations undermine the cost-effectiveness of EU climate policy and are unlikely to affect total emissions.

The proposed reforms in Table 2 suggest that EU climate policy should move towards uniform pricing of GHG emissions, thereby promoting cost-effectiveness. An in-depth discussion of the reforms can be found in Brøns-Petersen and Andersen (2025).

Are the Commission's omnibuses sufficient?

To date, the EU Commission has issued 8 omnibus packages aimed at simplifying the regulatory framework to strengthen competitiveness (European Council, n.d.). Only one of these is directly related to climate policy. The omnibus on sustainability relaxes reporting requirements for companies. Additionally, the implementation of some regulations has been postponed. In isolation, this is positive progress. However, it is not nearly enough. Fundamentally, corporate sustainability reporting is redundant and will not affect the EU's total GHG emissions. Therefore, corporate sustainability reporting should be abolished completely. Overall, these efforts are insufficient to achieve cost-effectiveness.

The Commission's proposal for achieving the 2040 climate target

The Commission has proposed flexible measures to reach its climate targets. One such measure is to include permanent carbon removals in the ETS – a measure previously recommended in an EPICENTER report (Brøns-Petersen and Andersen 2025). This would enhance the cost-effectiveness of climate policy by incentivising carbon removals at the same rate and under the same conditions as GHG abatement. This is a positive first step towards reforming EU climate policy.

Can gas independence be obtained while pursuing climate targets in the EU?

Climate, energy, and security policies are all interconnected. The EU pursues independence from Russian energy, including gas. The question is whether it is realistic to continue pursuing ambitious climate targets while also seeking gas independence. It is well established in economic sciences, that each policy problem requires at least one instrument (e.g., a tax) – a principle known as the Tinbergen rule (Tinbergen 1952). Therefore, advocating for gas independence is not an argument in favour of relaxing climate targets. On the contrary, gas independence should be pursued cost-effectively. The price system remains the most effective means of ensuring efficient resource allocation. Therefore, to achieve gas independence, a tax (or even a ban) on Russian gas would be

the most effective measure. The Council and Parliament have agreed to phase out Russian gas imports and introduce a full ban in the coming years (European Council, n.d.).

Other approaches, such as support for renewable energy, are not cost-effective. On the contrary, increased use of renewable energy will, all else being equal, increase demand for gas, as a flexible energy source to balance variability in an energy system otherwise based on solar and wind power.

If the appropriate instruments are used, there should be no inconsistency in pursuing both climate targets and gas independence simultaneously.

Conclusion

The EU already has the framework, in the form of the ETS, to pursue a cost-effective green transition and achieve net zero by 2050. The overarching objective of climate policy should be to ensure consistent pricing of all GHG emissions across member states, sectors, and uses. However, reform of the current climate policy is needed to achieve this. In the long run, all GHG emissions should be included in a single ETS. In the shorter term, the focus should be on abolishing damaging double regulation, including sector-specific targets, such as the phase-out of ICEs and overlapping regulations under the ETS2 and the ESR. Simplification efforts to date have been insufficient to ensure a cost-effective green transition in the EU. A comprehensive reform of climate policy would improve competitiveness and benefit businesses and citizens in the EU.

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