

European Union climate & energy package

European leaders are under pressure to strike a deal on the EU climate and energy legislative package, the EU's contribution to the post 2012 Kyoto Protocol process, but the resolve to meet the self-imposed December 2008 deadline to do so appears to be softening, despite the French Presidency's efforts to keep up momentum.

The EU has been and continues to be one of the strongest proponents of the UN Kyoto Protocol. It is a top priority amongst European leaders that the EU play a leading role in the "crunch" international climate talks in Poznań, Poland from 1 to 10 December 2008 and Copenhagen, Denmark at the end of 2009ⁱ. To achieve this, the EU negotiators need a strong mandate from the three main EU institutions responsible for setting EU law and policy, namely the European Commission, European Parliament and Council. But this is not an area where the EU has strong Treaty competences and so a mixture of carrots and sticks are needed to keep all Member States at the negotiating table. It is also important to note the other legislative proposals that are on the negotiating table that interrelate to the package. Taken together, the negotiators hope to showcase to the world at Poznań and Copenhagen as comprehensive a legislative framework as possible, that will deliver sustainable economic development in the EU and a persuasive contribution to the global effort.

- the third phase of the EU's emissions trading scheme (ETS phase 3)ⁱⁱ, including an extension to aviation during ETS phase 2.ⁱⁱⁱ
- the effort sharing mechanism^{iv} - which covers industries that are not (yet) included in the ETS, the allocation between the Member States according to their level of economic development (GDP), as well as the offsetting mechanism from investment in mitigation and adaptation projects in (principally less developed) countries,
- separate initiatives to reduce dependence on fossil fuels through commitments to invest in emissions reducing measures for cars^v, in renewables^{vi} and emerging technologies^{vii}, by both private finance and governmental intervention^{viii}. There are also interlinking reviews of directives that will also have a significant impact on the EU's Kyoto effort - including the recast of existing air quality directives,^{ix} as well as a review of the fuel quality directive^x, which includes the highly emotive debate on biofuels.
- on-going negotiations on a package to liberalise the European energy market, which is bogged down following an agreement on unbundling in June, as well as upcoming energy efficiency proposals, which are expected in December 2008. The new proposals may include new measures to "upgrade" the currently non-binding EU energy efficiency goal to mandatory targets.

The package is now before the European Parliament (EP) and national governments in the Council, who must jointly agree to adopt the legislation put forward by the European Commission, by introducing, if necessary, compromise amendments. Closing a deal is far from straightforward, not least as the intricate EU decision-making process has its own dynamic and the interlinkages between the separate proposals are not always self-evident. The consequences of this package are so politically charged that potential coalitions have fractured along intersecting political, national and sectoral lines. A delay into the new year is more probable than the French Presidency would like to publically admit.



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Sticking points

The package contains measures that would *significantly alter the current regulatory regime* affecting greenhouse gas emitting installations, but also other sectors including financial services (whose interests include CDM projects, commodity and commodity derivatives as well as carbon trading). The following points are particularly sensitive:

The cap

- The EU ETS is a “cap and trade” system. The overall level of emissions allowed is set at the beginning of the trading period, but within that limit, participants can buy and sell allowances as they require. The European Commission proposes to reduce EU emissions by 20% by 2020, based on 1990 levels. Should other industrialised countries undertake comparable reductions following international negotiations, it proposes automatically increasing the commitment to 30%. Several Member States as well as the Industry Committee of the EP would prefer to assess any international agreement before committing to this new target.

Allocation of allowances

- It is perhaps unsurprising that there should be great discussion over the reference period chosen to allocate allowances, and where the boundary lies between installations caught by ETS and those outside of it. Newer Member States are particularly unhappy with the base year 2005 as they claim that much of their activity to reduce emissions took place before accession to the EU and so would prefer the base year to be set at 1990, or an average of several years. Around half of the Member States and a number of MEPs are also understood to be unwilling to include small installations into the ETS. A possible compromise could be to raise the threshold from the proposals to include installations that emit 10 000 tonnes to 25 000 tonnes.

100% auctioning for the power sector from 2013

- Around half of the Member States, particularly, but not only the less wealthy, object to plans for 100% auctioning for the entire EU power sector as they say this will push electricity prices to unacceptable levels.
- Others are concerned about whether the auction revenues should go – to national coffers or back to industry, whether the revenue should be ring fenced for mitigation and adaptation projects and what percentage should go towards assisting developing countries. The EP is expected to suggest that a fund be established for developing countries which Member States could opt in (coalition of the willing). Member States are unsurprisingly mostly unwilling to accept mandatory earmarking.
- Energy intensive industrial sectors have mounted a sustained campaign against auctioning, making their cause one of the most hotly debated. Rather pessimistically, they doubt a global deal is achievable and claim that auctioning would seriously harm both EU competitiveness and expose them to potential financial ruin due the likelihood that foreign firms in their sector will not have to factor emissions costs in their prices. All the EU institutions are taking this threat seriously. Whereas the Commission wants to wait until June 2010 before coming up with criteria to ascertain which industries are truly vulnerable, for fear that talk of “carbon leakage” will sour global negotiations, the other institutions would prefer to initiate work on this now. In addition, the French Presidency has opened discussion on the possibilities of a border tariff, (which may or may not be WTO compatible). There appears to be an emerging consensus that should a satisfactory set of criteria emerge to identify sectors vulnerable to “carbon leakage”, up to 100% free allocation may be an acceptable option.

Effort sharing

- Most Member States have raised questions over the use of GDP as a determining factor, however, this points to a wider issue of how best to measure wealth in the EU (and is a perennial question in, for instance, the allocation of the structural funds. Other indicators may produce a ‘fairer’ result, but are not sufficiently robust to seriously rival GDP, however blunt a measurement it may be in reality.

Sectors not currently in the ETS

- Forestry. Integrating forestry in some form is likely to be part of the overall agreement as both the EP and the Council have called on the European Commission to come up with proposals, which are expected before the end of the month.
- Maritime emissions. Consensus appears to be forming in the EP and with several Member States over inclusion of maritime emissions in both the ETS and the effort sharing decision. This is a clear signal to the International Maritime Organisation [IMO] that unless work progresses on its emissions strategy^{xi}, the EU will break ranks and impose its own solution.
- Road transport. This appears to be off-limits as a discussion under the package, but cars will be subject to separate but related deal making over CO₂ for new passenger cars and the fuels quality directive.

Offsetting emissions in the EU

- No one appears to dispute the economical reality or even necessity of offsetting but concerns centre around what constitutes a suitable percentage of permissible credits, and the link with the UN CDM-JI projects.
- There are also continued doubts over the quality of projects undertaken overseas. In particular ETS should not replace funding for projects that would have taken place anyway. A number of MEPs have expressed support for the “Gold Standard” as a suitable method to monitor, measure and verify such projects.

Emerging technologies

- Proponents for carbon capture and storage have convinced leading MEPs to table amendments which would divert up to 500 million allowances from the new entrants reserve in the ETS to go towards deployment. Others, such as the Greens, do not agree, saying this would preclude investment in renewables and energy efficiency measures. CCS would encourage continued and

prolonged use of coal, and has yet to be tested to scale. However, a consensus seems to be building that it represents a viable and pragmatic intermediate step in the right direction.

Biofuels

The fuel quality directive is currently being revised and the climate change package's renewables directive contains provisions on biofuels. This is an example of the interlinkages between the package and other legislation. As the fuel quality directive negotiation is more advanced, it is expected to heavily influence the outcome of the renewables directive negotiation. The key issues are:

- The proposed article 7a contains an obligation that fuel suppliers reduce their fuels' lifecycle greenhouse gases by 10% by 2020. Some Member States would like to simply delete the whole article. Others are 'cautious' of the impact EU targets might have on food prices, land use etc.
- Sustainability criteria. A number of Members of the European Parliament and Member States are reluctant to commit to the above mentioned target before defining some basic sustainability criteria for the production of biofuels. It is expected that such criteria would be set in the fuels quality directive negotiations, and then extended to the renewables directive. In addition to a number of basic biodiversity and social criteria, MEPs would like to see a target for biofuels to deliver life-cycle CO² savings of at least 50% compared to conventional fuels, with immediate effect^{xii}. Member States appear to want a less radical target. In Council, a position seems to be forming that Member States could accept 35% with immediate effect and a 50% reduction by 2013. Media reports suggest a slightly different formula (50% by 2017).

Next steps

European Parliament

In the European Parliament, the package has been discussed in several committees, with the Environment Committee (ENVI) in the lead. All the other committees involved have now adopted their opinion. The most important vote will take place in the ENVI Committee on 7 October 2008, with the highest profile report drafted by Avril Doyle, the 'rapporteur' for ETS phase 3. A vote will then take place at the plenary session of the European Parliament in December 2008.

Council

The French hold the Presidency of the EU until the end of the year, which puts them in a key position as chair of Council meetings and deal broker. It is a priority at the highest level of French government that they achieve overall agreement by December. Aside from frequent meetings between diplomats from the Permanent Representations of the Member States, the Council secretariat and the European Commission, the French Presidency has also tabled a series of "orientation debates" between now and the end of the year in the Energy and Environment Councils as well as 15-16 October and 11-12 December's European Council meetings. The French Presidency will start negotiating a political agreement with the EP Rapporteur after the vote in the ENVI Committee, in order to try to reach a compromise between the EP and the Council for the end of the year.

ⁱ Drafting the text of the treaty was expected to begin this summer.

ⁱⁱ Proposal for a Directive amending Directive 2003/87/EC – COM(2008)16

ⁱⁱⁱ Proposal for Directive of the European Parliament and of the Council amending Directive 2003/87/EC so as to include aviation activities in the scheme for greenhouse gas emission allowance trading within the Community - COM(2008)221

^{iv} Proposal for a Decision of the European Parliament and of the Council on the effort of Member States to reduce their greenhouse gas emissions to meet the Community's greenhouse gas emission reduction commitments up to 2020 - COM(2008)30

^v Proposal for a Regulation of the European Parliament and of the Council setting emission performance standards for new passenger cars as part of the Community's integrated approach to reduce CO² emissions from light-duty vehicles - COM(2007)856

^{vi} Proposal for a Directive of the European Parliament and of the Council on the promotion of the use of energy from renewable sources - COM(2008)19

^{vii} Proposal for a Directive of the European Parliament and of the Council on the geological storage of carbon dioxide – COM(2008)18

^{viii} COMMUNITY GUIDELINES ON STATE AID FOR ENVIRONMENTAL PROTECTION – OJ 2008/C 82/01

^{ix} Notably the Integrated Pollution Prevention Control (IPPC) and Large Combustion Plant (LCP) Directives - Proposal for a Directive of the European Parliament and of the Council on industrial emissions (integrated pollution prevention and control) (Recast) - COM(2007) 843 final

^x Proposal for a Directive of the European Parliament and of the Council amending Directive 98/70/EC as regards the specification of petrol, diesel and gas-oil and the introduction of a mechanism to monitor and reduce greenhouse gas emissions from the use of road transport fuels and amending Council Directive 1999/32/EC, as regards the specification of fuel used by inland waterway vessels and repealing Directive 93/12/EEC - COM(2007)18

^{xi} An IMO study of greenhouse gas emissions has estimated that emissions from the global fleet would increase dramatically in the next 20 years as globalisation leads to increased demand for bigger, faster ships. Without action the IMO predicts that by 2020, emissions from ships would increase up to 72%.

^{xii} In the proposed renewable energy directive, the Commission puts forward 35% by 2013.

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