ALERT MEMORANDUM

Provisional Agreement On European Climate Law

April 27, 2021

On April 21, 2021, European Union negotiators reached a provisional agreement on a European Climate Law, in the form of a new Regulation. The EU reaffirmed its commitment to achieve climate neutrality by 2050, and set an intermediate target of reducing net greenhouse gas ("GHG") emissions by at least 55% by 2030, compared to 1990 levels.

The provisional agreement on the Commission's amended proposal[1] for a new Regulation was timed to precede a global Leaders Summit on Climate convened by U.S. President Biden. The European Climate Law was heralded as a key goal of the von der Leyen Commission in its October 2019 Political Guidelines, as part of the EU Green Deal, a comprehensive roadmap for climate action and sustainable investment.[2] In addition to setting emissions targets, the European Climate Law provides for the wholesale review of EU legislation to work towards those ends, and arms the Commission with various tools to support the EU's transition to a green economy. The final text of the Regulation, which would have direct effect and would be adopted by qualified majority, is yet to be published.

The Biden administration also announced on April 22, 2021 its intention to cut GHG emissions by 50-52% by 2030, compared to 2005 levels. In a similar vein, in December 2020, the United Kingdom committed to cut GHG emissions by at least 68% by 2030, compared to 1990 levels, which it has since revised to a 78% reduction by 2035, compared to 1990 levels. Both the United Kingdom and the United States, like the EU, committed to achieving net zero emissions by 2050. China aims to achieve that goal in 2060.

If you have any questions concerning this memorandum, please reach out to your regular firm contact or the following authors.

LONDON

Maurits Dolmans
+44 20 7614 2343
mdolmans@cgsh.com

Emma O'Brien
+44 20 7614 2397
eobrien@cgsh.com

BRUSSELS

Géraldine Bourguignon
+32 2287 2143
gbourguignon@cgsh.com

PARIS

Laurie Achtouk-Spivak
+33 1 40 74 68 00
lachtoukspiavk@cgsh.com

Robert Garden
+33 1 40 74 68 00
rgarden@cgsh.com

ROME

Clara Cibrario Assereto
+39 06 6925 2225
ccibrarioassereto@cgsh.com

ABU DHABI

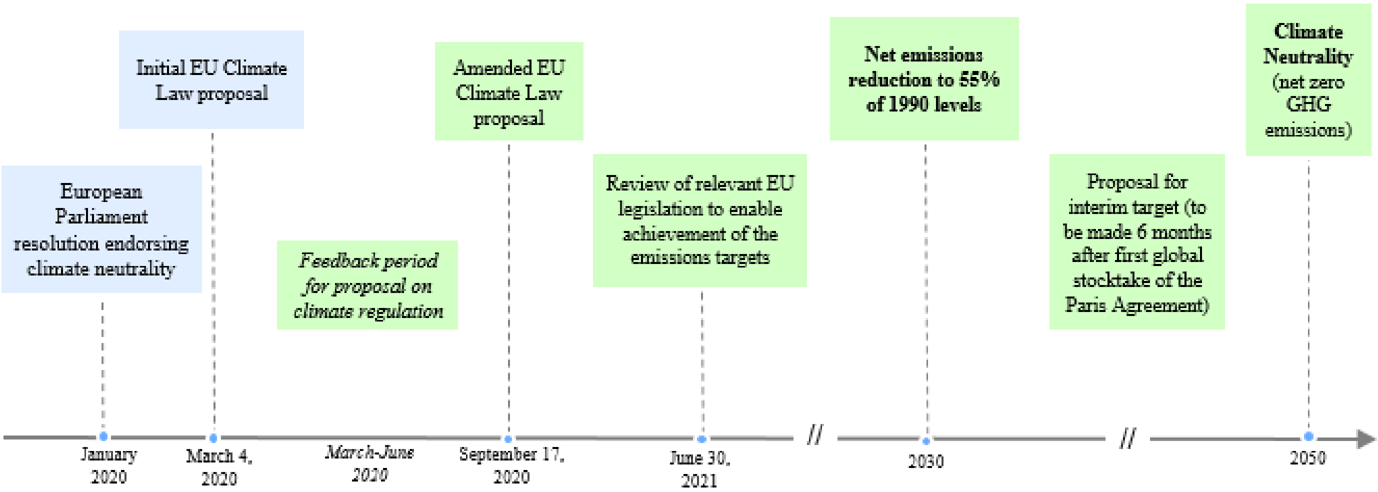
Chris Macbeth
+971 2 412 1730
cmacbeth@cgsh.com

1 The original proposal of Regulation (EU) 2018/1999 (European Climate Law) (March 4, 2020), available here, was updated following an impact assessment on the possible increase of the 2030 target, and resulted in the amended proposal (September 17, 2020).

2 For further information, *see* our alert memorandum "A Sustainable Recovery for Europe: The EU's Green Deal".

© Cleary Gottlieb Steen & Hamilton LLP, 2021. All rights reserved.
This memorandum was prepared as a service to clients and other friends of Cleary Gottlieb to report on recent developments that may be of interest to them. The information in it is therefore general, and should not be considered or relied on as legal advice. Throughout this memorandum, "Cleary Gottlieb" and the "firm" refer to Cleary Gottlieb Steen & Hamilton LLP and its affiliated entities in certain jurisdictions, and the term "offices" includes offices of those affiliated entities.

At a glance, the timeframe of the adoption of the European Climate Law, and for its goals, is as follows:



I. EMISSIONS TARGETS

With a view to ultimately achieving climate neutrality in the EU by 2050, the European Climate Law is expected to set an intermediate target of a reduction of net GHG emissions of at least 55% by 2030, compared to 1990 levels, including emissions and removals. The net GHG emissions target translates to a gross reduction of 52.8%, when excluding the removal of GHG emissions via carbon sinks such as agriculture and forestry.[3]

The 2050 target, to which the European Parliament agreed in January 2020,[4] is collective and relates to Union-wide emissions, without requiring net zero emissions at the level of each individual Member State.[5] According to the Commission press release, negotiators committed to negative emissions in the EU after 2050.[6]

To enhance the removal of GHGs by means of carbon sinks, the European Climate Law will propose the adoption of a more ambitious Regulation on the inclusion of GHG emissions from land use, land use change and forestry (LULUCF) into the 2030 climate and energy framework ("LULUCF Regulation").[7] The LULUCF Regulation establishes rules under which Member States would be required to balance deforestation by planting new trees, and to set measures to boost carbon absorption by forests, croplands and grasslands. The Commission will publish proposals for revising the LULUCF Regulation in line with the new emissions targets in June 2021.

Where progress towards these ends is inadequate or measures adopted are inconsistent with those targets, intermediate targets may be adopted. Under the provisional agreement, the Commission agreed to propose an interim target for 2040 within six months

3 European Commission Impact Assessment, accompanying the European Commission Communication 'Stepping up Europe's 2030 climate ambition' (September 17, 2020), Part 1, p. 52.

4 Resolution of the European Parliament on the European Green Deal (2019/2956(RSP)) (January 15, 2020).

5 Proposal for a Regulation of the European Parliament and of the Council establishing the framework for achieving climate neutrality and amending Regulation (EU) 2018/1999 (European Climate Law) (March 4, 2020), Article 2(1).

6 Commission Press Release, "Commission welcomes provisional agreement on the European Climate Law" (April 21, 2021).

7 LULUCF Regulation (May 30, 2018).

after the first global stocktake under the Paris Agreement (which will take place in 2023), if considered appropriate at that stage. At the same time, the Commission will publish a projected indicative EU GHG budget for 2030-2050, setting out the indicative total volume of net GHG emissions that are expected to be emitted in that period without putting the EU's commitments under the Paris Agreement at risk.[8]

Continuous monitoring will be key to working towards such targets. Negotiators for the European Parliament and the Council have therefore agreed to the establishment of a European Scientific Advisory Board on Climate Change, which will provide independent scientific advice in support of exercising the required scrutiny.

II. Ongoing Review of EU Law

The Commission's press release notes that the European Climate Law aims to ensure "*strong coherence across Union policies with the climate neutrality objective*".[9] This reiterates the EU's intention to review existing EU frameworks in light of the green transition, in line with previous publications.[10]

To some extent, this process is already underway. In EU competition law, for example, the review of the Horizontal Block Exemption Regulations in 2010 removed environmental agreements from scope. The Commission is now reviewing whether to reinsert guidelines on sustainability agreements.[11] However, the European Climate Law should ensure that reviews of this kind already underway on a piecemeal basis occur comprehensively.

According to the Commission, negotiators have agreed to engage with industry sectors to prepare sector-specific roadmaps charting the path to climate neutrality in different areas of the economy.

III. Legislative Backdrop

In addition to any forthcoming amendments to EU legislation following the Commission's review process, the European Climate Law has been agreed amidst a wave of regulatory reforms. Below is an overview of the most relevant recent pieces.

EU Taxonomy Regulation

This Regulation entered into force on July 12, 2020.

It introduces an EU-wide taxonomy (or combined glossary and classification system) of environmentally sustainable activities, as well as new disclosure requirements for certain financial services firms and large public interest entities.[12]

EU Taxonomy Climate Delegated Act

Political agreement on the text of the Delegated Act was reached on April 21, 2021.[13]

The Delegated Act introduces the first set of technical screening criteria to define which activities contribute substantially to two of the environmental objectives under the EU Taxonomy Regulation (climate change adaptation and climate change mitigation).

8 Council of the European Union Press release, "European climate law: Council and Parliament reach provisional agreement" (April 21, 2021).

9 Commission Press Release, "Commission welcomes provisional agreement on the European Climate Law" (April 21, 2021).

10 See the Commission's amended proposal of September 17, 2020, which provided that "[b]*y 30 June 2021, the Commission shall review relevant Union legislation in order to enable the achievement of the target set out in paragraph 1of this Article and the climate-neutrality objective set out in Article 2(1) and consider taking the necessary measures, including the adoption of legislative proposals, in accordance with the Treaties*" (Amended Proposal for a Regulation of the European Parliament and of the Council establishing the framework for achieving climate neutrality and amending Regulation (EU) 2018/1999 (European Climate Law) (September 17, 2020), Recital 17.

11 *See* Maurits Dolmans, 'Sustainable Competition Policy and the "Polluter Pays" Principle' in *Competition Law, Climate Change & Environmental Sustainability* (Concurrences, 2020) (ed. Simon Holmes, Dirk Middelschulte, Martijn Snoep) [link to draft version].

12 *See* our alert memorandum.

13 Commission Press Release, "Sustainable Finance and EU Taxonomy: Commission takes further steps to channel money towards sustainable activities" (April 21, 2021).

The question of the inclusion of natural gas and nuclear power in the EU Taxonomy has been delayed and will be confirmed in due course by the Commission, following further assessments.

Corporate Sustainability Reporting Directive

A proposal for a Corporate Sustainability Reporting Directive was tabled by the Commission on April 21, 2021.[14]

The proposed Directive would revise and strengthen existing rules under the Non-Financial Reporting Directive, and extend requirements to report on sustainability and climate risk exposure to all large companies and all listed companies.

Sustainable Finance Disclosure Regulation

Sustainability-related disclosures that are specific to the financial sector have become mandatory in the EU effective on March 10, 2021.

The Sustainable Finance Disclosure Regulation ("SFDR") requires asset managers and investment advisors to provide information on how sustainability risks are integrated in their investment decision-making processes or advice, and to disclose to investors the way in which ESG risks are likely to impact the returns of their investments, as well as (for larger firms) a description of the principal adverse impacts of investment products on sustainability factors.

Corporate Due Diligence and Accountability

A proposal for a Directive on mandatory human rights, environmental and good governance due diligence is planned to be adopted by the Commission in the second quarter of 2021.

This Directive is expected to require companies operating in the EU to carry out risk assessments across their value chains, address any identified human rights, state governance, and environmental issues, and disclose information on any adverse impacts and related remedial plans.

Six amending Delegated Acts

The six Delegated Acts were tabled on April 21, 2021 and propose further regulation in the financial sector, focusing on the following:[15]

- The sustainability risks and sustainability factors to be taken into account for Undertakings for Collective Investment in Transferable Securities ("UCITS").[16]

- The sustainability risks and sustainability factors to be taken into account by Alternative Investment Fund Managers.[17]

- The integration of sustainability factors, risks and preferences into the product oversight and governance requirements for insurance undertakings and insurance distributors, and into the rules on conduct of business and investment advice for insurance-based investment products.[18]

---

14 Commission Press Release, "Sustainable Finance and EU Taxonomy: Commission takes further steps to channel money towards sustainable activities" (April 21, 2021).

15 Commission Press Release, "Sustainable Finance and EU Taxonomy: Commission takes further steps to channel money towards sustainable activities" (April 21, 2021).

16 Commission Delegated Directive (EU) amending Directive 2010/43/EU as regards the sustainability risks and sustainability factors to be taken into account for Undertakings for Collective Investment in Transferable Securities (UCITS) (April 21, 2021).

17 Commission Delegated Regulation (EU) amending Delegated Regulation (EU) No. 231/2013 as regards the sustainability risks and sustainability factors to be taken into account by Alternative Investment Fund Managers (April 21, 2021).

18 Commission Delegated Regulation amending Delegated Regulations (EU) 2017/2358 and (EU) 2017/2359 as regards the integration of sustainability factors, risks and preferences into the product oversight and governance requirements for insurance undertakings and insurance distributors and into the rules on conduct of business and investment advice for

- The integration of sustainability risks into product governance obligations.[19]

- The integration of sustainability risks in the governance of insurance and reinsurance undertakings.[20]

- The integration of sustainability factors, risks and preferences into certain organizational requirements and operating conditions for investment firms.[21]

Carbon Border Adjustment Mechanism

Commission adoption of a carbon border adjustment mechanism is planned for the second quarter of 2021.

This initiative intends to counteract the risk of carbon leakage through importation from, or transfer of production from the EU to, countries with less stringent emissions standards.[22]

Energy Taxation Directive

Revision of the Energy Taxation Directive is planned for the second quarter of 2021.[23] The main objectives of revising the Directive are:

- Aligning taxation of energy products and electricity with EU energy and climate policies, to contribute to the EU 2030 energy targets and climate neutrality by 2050; and

- Preserving the EU single market by updating the scope and the structure of tax rates, and rationalizing the use of optional tax exemptions and reductions.

IV. FURTHER INFORMATION

We monitor the evolving European framework related to sustainability and parallel developments globally. For more information, including thought leadership publications, see the website of our Sustainability Practice Group, available here.

…

CLEARY GOTTLIEB

insurance-based investment products (April 21, 2021).

19 Commission Delegated Directive amending Delegated Directive (EU) 2017/593 as regards the integration of sustainability factors into the product governance obligations (April 21, 2021).

20 Commission Delegated Regulation amending Delegated Regulation (EU) 2015/35 as regards the integration of sustainability risks in the governance of insurance and reinsurance undertakings (April 21, 2021).

21 Commission Delegated Regulation amending Delegated Regulation (EU) 2017/565 as regards the integration of sustainability factors, risks and preferences into certain organisational requirements and operating conditions for investment firms (April 21, 2021).

22 *See* European Commission, EU Green Deal (carbon border adjustment mechanism).

23 *See* European Commission Published Initiative, EU Green Deal – Revision of the Energy Taxation Directive.