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Subject:	Non-ETS sectors: a) Proposal for a Regulation of the European Parliament and of the Council on binding annual greenhouse gas emission reductions by Member States from 2021 to 2030 for a resilient Energy Union and to meet commitments under the Paris Agreement and amending Regulation No 525/2013 of the European Parliament and the Council on a mechanism for monitoring and reporting greenhouse gas emissions and other information relevant to climate change (First Reading) b) Proposal for a Regulation of the European Parliament and of the Council on the inclusion of greenhouse gas emissions and removals from land use, land use change and forestry into the 2030 climate and energy framework and amending Regulation No 525/2013 of the European Parliament and the Council on a mechanism for monitoring and reporting greenhouse gas emissions and other information relevant to climate change (First Reading) - Progress report

I. INTRODUCTION

1. At its meeting on 23-24 October 2014, the European Council agreed on the 2030 climate and energy policy framework for the European Union and endorsed a binding EU target of an at least 40% domestic reduction in greenhouse gas emissions by 2030 compared to 1990[1]. This target also represents the Intended Nationally Determined Contribution (INDC) of the EU and its Member States, which was submitted to the UNFCCC on 6 March 2015. The European Council conclusions contain specific guidance, *inter alia*, on the methodology to be used for setting the national emission reduction targets for 2030 in the non-ETS sectors, and on the availability and use of flexibility instruments within those sectors.

2. On 20 July 2016, the Commission adopted two legislative proposals on the contribution of the non-ETS sectors towards the overall effort: on binding annual greenhouse gas emissions reductions by Member States from 2021 to 2030 ("Effort Sharing Regulation")[2] and on the inclusion of greenhouse gas emissions and removals from land use, land use change and forestry into the 2030 climate and energy framework ("LULUCF Regulation")[3]. Together with the proposal for the revision of the EU ETS, they are intended to ensure achievement of the EU's overall target for greenhouse gas emission reductions by 2030 and the commitments of the EU and the Member States under the Paris Agreement.

3. The proposal for an Effort Sharing Regulation (ESR) sets the national reduction targets based on relative GDP per capita, with the targets for Member States with a GDP per capita above the EU average adjusted to reflect cost-effectiveness within that group. The proposal maintains existing flexibilities (banking and borrowing, transfers between Member States), and proposes two new flexibilities: a limited use of net removals from certain LULUCF accounting categories towards the targets in the effort-sharing sectors; and the possibility for certain Member States to use a limited number of ETS allowances (in total 100 million) to offset emissions in the effort sharing sectors.

[1] Doc. EUCO 169/14
[2] Doc. 11483/16 + ADD 1 + ADD 2 + ADD 3.
[3] Doc. 11494/16 + ADD 1 + ADD 2 + ADD 3.

4. The aim of the proposed LULUCF Regulation, which builds on the existing EU-wide accounting rules laid down in Decision No 529/2013/EU, is to define how to include the LULUCF sector in the 2030 climate and energy policy framework. The proposal requires Member States to ensure that accounted greenhouse gas emissions and removals stay in balance and that the overall LULUCF sector does not generate net emissions ("no-debit rule") and sets out accounting rules for specific land use sectors. Several flexibilities are included to help Member States ensure compliance with that rule: the possibility to use excess allocations from the ESR, compensating emissions from one land category with removals from another, accumulating net removals over the period 2021-2030, and trading of excess removals among Member States. The proposal also introduces a new EU governance process for the determination of forest management reference levels.

5. The Council (Environment) held a policy debate on the two proposals on 17 October 2016, and took note of a report by the Slovak Presidency on the state of play at its meeting on 19 December 2016. Work at technical level has continued throughout the Maltese Presidency. The latest Presidency compromise texts, which were discussed at the meetings of the WPE on 29 (LULUCF) and 30 May (ESR), are attached to documents 9699/17 and 9611/17 respectively.

6. The European Parliament's Committee on the Environment, Public Health and Food Safety (ENVI) voted on the draft report on the ESR proposal on 30 May 2017. The Committee vote on the LULUCF proposal is scheduled on 22 June 2017. The plenary votes on both proposals are expected to take place in July.

7. The Economic and Social Committee and the Committee of the Regions delivered their opinions on both proposals on 14 December 2016 and 22-23 March 2017, respectively.

8. In the following sections, the Presidency sets out the progress achieved so far on the two proposals and identifies the most important outstanding issues.

II. EFFORT SHARING REGULATION

General

The key issues of the proposal were identified early on in the discussions within the Council. While the proposed national greenhouse gas emissions reduction targets for 2030 were generally not called into question, many delegations considered that further work was needed on other central elements of the proposal, in particular the starting point of the linear reduction trajectory and the so-called "new" flexibilities, in order to ensure the overall balance of the proposal. However, despite detailed discussion of those issues at Working Party level, including examination of various alternatives to the approach proposed by the Commission, the delegations' positions on the key issues remain divided. Therefore, the Presidency recently submitted a compromise suggestion based on the introduction of a new element into the discussions, namely an additional safety reserve for Member States, which aims to address the concerns of a number of delegations without changing the central elements of the Commission proposal.

The state of play on the above-mentioned key issues is described in the following. Other issues which remain under discussion include, *inter alia*, methodological issues concerning determination of annual emission allocations (Article 9), and the review (Article 14) particularly as regards the link with the Paris Agreement timeline.

Main issues

A. Starting point of the linear reduction trajectory

Article 4 and Annex I of the Commission proposal set out the Member States' greenhouse gas emission reductions in 2030. The annual emission limits are determined based on a linear trajectory, starting in 2020, from the average emissions for 2016-2018 based on the most recent reviewed GHG emission data.

The definition of the starting point has significant impacts on the expected surplus or shortage of emission allocations in the Effort Sharing sectors in the period from 2021 to 2030, and delegations' positions remain divided on the issue. Many delegations support the Commission proposal on the starting point. For some delegations, the choice of average emissions for 2016-2018 as the starting point does not adequately take into account early efforts to reduce emissions, and some of them suggest that the Member States' 2020 targets should be used as the basis instead. Others agree with the Commission's assessment that the 2020 target value as the starting point would result in a too large surplus of emission allocations and therefore lead to a risk of not achieving the 2030 target. A third option has also been suggested: should the approach as proposed by the Commission lead to a Member State's emission allocation for 2021 exceeding its 2020 target, the 2020 target value of that Member State should be used instead. Some delegations would prefer the trajectory to start in 2021 instead of 2020, as proposed by the Commission. Given that none of the alternatives to the approach proposed by the Commission on the starting point are supported by a majority of the delegations, the latest Presidency text does not propose substantive changes in this Article.

B. Adjustment to the allocation for certain Member States

To address distributional impact concerns of those Member States which were allowed to increase emissions in 2020 compared to 2005, Article 10(2) and Annex IV of the Commission proposal provide for an adjustment to the allocation in 2021 for Member States with both a positive limit under the Effort Sharing Decision and increasing annual emission allocations between 2017 and 2020. The adjustment increases the ESR allocation for the Member States concerned by an amount equal to the increase in allocations over the period 2017-2020 under the existing Effort Sharing Decision compared to their average allocation in the period 2016-2018. However, several of the benefitting Member States consider that the proposed method of adjustment is insufficient in light of previous efforts made up to 2020.

C. Continuation of existing flexibilities

The flexibilities available to Member States to achieve their annual limits include flexibility over time through banking and borrowing of Annual Emission Allocations (AEAs) within the commitment period and flexibility between Member States through transfers of AEAs (Article 5 of the Commission proposal). A number of delegations have suggested that those flexibilities should be further enhanced, as called for by the European Council in its October 2014 conclusions. The Presidency has therefore proposed to raise the limit for borrowing from 5% to 10% during the first 5-year allocation period, and to include a new provision in the text mentioning the possibility of project-based transfers between Member States.

D. One-off flexibility

Article 6 and Annex II of the Commission proposal provide for a new one-off flexibility through the cancellation of up to 100 million EU ETS allowances in order to facilitate the achievement of targets for Member States with national reduction targets significantly above both the Union average and their cost-effective reduction potential, as well as for Member States that did not allocate any allowances for free to industrial installations in 2013. Given that so far suggestions to change the Commission proposal on the one-off flexibility with regard to its overall maximum amount, eligibility for and level of access to it, have gathered little support in the Working Party, the latest Presidency compromise text does not include any changes to the approach proposed by the Commission. However, the Presidency text does introduce more flexibility for eligible Member States by allowing them to revise their initial decision from 2019 on their intended use of the flexibility on two occasions later in the period.

E. LULUCF flexibility

In its Article 7 and Annex III, the proposal provides for the possibility for Member States to use up to 280 million net removals from the accounting categories deforested land, afforested land, managed cropland and managed grassland to offset emissions in the ESR sectors. The new flexibility is available to all Member States but the distribution takes account of the relative share of agricultural emissions in the ESR. A few delegations are in favour of raising the overall amount of the flexibility. Some delegations are critical of the way in which Member States are divided into groups, considering this as arbitrary, and have suggested alternative approaches. Each of them would result in changes in the distribution among Member States of the overall flexibility. Linked to the discussions on the proposed LULUCF Regulation, a number of delegations consider that the possibility to use credits from forest management under this Article should not be deferred to a later time, as proposed by the Commission, but that it should be available from 2021. At the present time, there has not been significant support for the various alternative approaches concerning the distribution of the flexibility. Therefore, the latest Presidency text does not propose any substantive changes to the Commission proposal on this Article.

F. Presidency proposal for an additional safety reserve

As mentioned in the foregoing, the latest Presidency compromise text proposes a new Article 10a on a safety reserve, which would be available at the end of the 2021-2030 period as an additional flexibility in case of real need of individual Member States. The reserve would not change the main features of the Commission proposal on Articles 4, 10 or 7. According to the Presidency compromise proposal, the reserve should only benefit Member States with a GDP per capita below the EU average in 2013 which will overachieve their 2020 targets and which have problems to achieve their 2030 emission target despite using other flexibilities provided for in the proposed Regulation. The reserve would be available to the Member States which fulfil all the required conditions, and the use of the reserve should not hinder the achievement of the EU's emission reduction target of 30% for the year 2030 in the sectors covered by the proposed ESR Regulation.

The availability of the reserve would moreover be dependent on the extent of the EU's overachievement of the EU's 2030 non-ETS target. Given that early action until 2020, and a real need for domestic target achievement, as well as the EU's achievement of the 2030 target are all important conditions, the amounts available to individual Member States cannot be fixed at the moment. However, the rules which translate these conditions into an objective distribution key should already be defined.

Delegations generally welcomed the Presidency's efforts to find a way a forward, and many of them recognised the merits of the proposed approach. However, delegations have requested more information and clarification on several important aspects of the proposed reserve, such as the total amount of the reserve, its availability and level of access for individual Member States, and its potential impacts on transfers between Member States.

The Presidency believes that such a reserve, tied to a set of clearly defined conditions and complementing the existing key elements of the Commission proposal, could help to solve a number of outstanding issues on other key parts of the proposal while safeguarding both its environmental integrity and key objective of ensuring the achievement of the EU's 2030 target in the non-ETS sectors. Therefore, the Presidency considers that future work on the proposal should focus on further detailed discussion of the new reserve.

III. LULUCF

General

There is a general support among delegations for inclusion of the LULUCF sectors as important and integral elements of the EU's 2030 climate and energy framework. However, many delegations are concerned with the overall balance of the proposal, in particular regarding the contribution of forests and sustainable forest management practices towards incentivising climate action, meeting their climate and energy commitments and consistency with achieving the long term objectives of the Paris Agreement. At the same time, the environmental integrity of the proposal, its transparency and credibility at the international level were raised during the discussions as the important principles.

It is the Presidency 's assessment that significant progress has been made on clarification of the text and comprehension of the outstanding issues of this complex proposal.

The following main issues can be identified from the discussions. Progress on these issues can be recorded, but they require further in-depth consideration.

Main issues

A. Forest reference levels and cap on the use of credits

The use of forest reference levels based on a historical reference period, i.e. 1990-2009, and setting a "cap" on the use of credits generated by managed forest land and in their LULUCF accounts, equal to 3.5% of the Member State's total emissions in its base year or period are the key elements of the Commission's approach towards the accounting for managed forest land.

A number of delegations support this approach, arguing that such an approach best ensures the environmental integrity of the proposal. Several other delegations, however, have instead called for alternative approaches, which would better reflect diversity in the circumstances among Member States in terms of their forest coverage, forest management, age of forests and natural conditions. In particular, setting forest reference levels based on historical reference periods may lead to a result where a sustainable and increasing use of forests becomes a source of emissions in accounting terms, while in reality they are generating a real net sink. They would therefore prefer an approach that brings about fair treatment towards all Member States and allows and promotes the development of policies for sustainable forest management based on their national circumstances.

In order to reconcile the differing positions, the Presidency has tabled a compromise which, while maintaining a baseline forest reference level, based on a historical - however more recent - reference period from 2000 to 2009, allows for <u>more flexibility</u> for Member States. Member States will thus have the option to <u>use a national threshold</u> provided that certain objective criteria are fulfilled. While reflecting national circumstances, this threshold will also provide for safeguards to ensure that it will be aligned with sustainable management of forests. Emissions which fall below such a national threshold, i.e. debits, should be discounted by a factor of [0,5]. Further, the national threshold will be determined by applying a harvest intensity of no greater than [80%] of the projected forest increment.

In respect of the cap on the use of credits generated by managed forest land, the Presidency proposes two alternative options: 1) redistribution of the cap based on forest area, or 2) a cap expressed as a percentage [3.5].

At this stage the Presidency compromise has not generated sufficient support form delegations. Those delegations who have supported the Commission approach, have concerns that the Presidency proposal will not sufficiently ensure environmental integrity. For other delegations, the proposal still poses a problem in terms of not reflecting the actual sinks created by sustainable forest management. Some of these delegations are however willing to continue work on the basis of the Presidency compromise, while others would prefer alternative options for approaches towards forests accounting. Some delegations have tabled alternative suggestions. Several delegations maintain their preference for deleting the cap on the use of credits or raising the cap.

B. Governance

Given the sensitivity of the forest reference level issue there has been a general concern among delegations about the use of delegated acts for setting future forest reference levels, as proposed by the Commission. The Presidency has therefore suggested the use of implementing acts in order to provide additional reassurance. Further, the Presidency has sought to clarify that the role of the Commission would be to provide a technical assessment only and to ensure that the calculations provided by the Member States are in accordance with the relevant provisions of the Regulation. While these suggestions were received positively, a number of delegations wish to further clarify the role of the Commission.

Other issues

The Presidency text maintains the scope of the proposal as proposed by the Commission. A number of delegations have called for inclusion of harvested wood products as a separate accounting category (and gross net accounting) and some would prefer that accounting for managed wetlands be mandatory. However, given that most delegations can support the Commission proposal with some delegations explicitly rejecting these alternative proposals, the Presidency has not changed the Commission text. In order to accommodate those delegations who have called for a distinct treatment of accounting for harvested wood products, the Presidency proposes adjustments which explicitly sets out the accounting of harvested wood products.

Some delegations have pleaded for more flexibility in setting the reference period or suggested different periods or base years for the specific accounting rules for managed cropland, grassland and wetland.

Upon request of some delegations, the Presidency has included a provision on accounting for forest biomass. While the inclusion of biomass has been widely welcomed, some delegations have questions on the exact content or feasibility of the provision.

Two delegations maintain their objection to having a separate target for the land use sector - the so called no debit rule - the commitment for each Member States to balance emissions and removals from the land-use sectors in two periods 2021-2025 and 2026 - 2030. They believe that LULUCF should only aim at establishing accounting rules and have concerns that this provision will set a precedent for inclusion of specific targets for other sectors.

IV. CONCLUSION

The Permanent Representatives Committee is invited to take note of the present progress report and forward it to the Council (Environment) with a view to its meeting on 19 June 2017.