

State of the European Green Deal The process of making Europe Fit for 55

Table of Contents

1. Introduction and Approach	2
2. Context: The Evolution of the EU Climate and Energy Policy.....	2
2.1 The 2020 Package	2
2.2 The Energy Union 2014-2019	2
2.3 The European Green Deal	3
3. The EGD Structure and Developments	3
3.1 Initial proposition.....	3
3.2 COVID-19 Recovery adjustments.....	4
3.3 The 2030 climate target plan	4
3.3.1 Agreement on the Climate Law	4
4. Substantive Elements: An Overview	5
4.1 CBAM.....	5
4.2 ETS – breaking down elements of the upcoming review.....	5
4.3 The EU sustainable finance agenda in the context of the EGD	6
4.3.1. The first EU sustainable finance strategy: 3 objectives and 10 action points.....	6
4.4. The EU renewed sustainable finance strategy.....	7
4.5. Hydrogen	7
4.6. Just Transition	8
5. State of play before the Fit for 55 publication	8

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1. Introduction and Approach

The EGD is now approaching a key point in time. This paper intends to provide a general overview of the EU Green Deal State of Play, including a brief review of the main EU energy and environmental milestones from the 2000 until today to enhance a better understanding of the massive legislative review expected for July 2021. A few days ahead of the “Fit-for 55 package” publication, this paper will also briefly address, the evolution and state of play of key integral parts of the EGD such as the EU-ETS, the introduction of a Carbon Border Adjustment Mechanism (CBAM), the EU sustainable finance agenda or the development of an EU hydrogen economy. This paper also intends to capture the evolutionary and transformational nature of the EGD, providing the reader an easy understanding of its past, present and future.

2. Context: The Evolution of the EU Climate and Energy Policy

The first elements of an EU Climate policy can be traced back to the 1990s, at a moment where climate issues were gaining momentum on the international political agenda.

In 1990, after the release of the first IPCC report, the EU Council agreed to stabilize EU GHG emissions at 1990 levels by 2000. While EU leaders did not specify which measures would have allowed the achievement of such target, the agreement triggered a discussion that eventually led to the three streams of EU climate policy, which are valid still today: emissions reduction, the promotion of renewable energy and improvements in energy efficiency.

Under the 1997 UNFCCC Kyoto Protocol, the EU committed itself to reduce GHG emissions by 8% during the 2008-2012 commitment period. On the back of what was agreed in Kyoto, EU climate policy entered an eventful phase. The 2000 European Climate Change Programme examined different policy options to tackle GHG emissions. In 2003, the European Emissions Trading Scheme (ETS) was launched, with national caps on emissions from power and industry sectors. Legislation on renewable energy and energy efficiency was also adopted.

2.1 The 2020 Package

In 2007, EU member states committed to a set of three targets to be achieved by 2020 under the 2020 climate & energy package: a 20% cut in GHG emissions from 1990 levels, 20% of EU energy from renewable sources and 20% improvement in energy efficiency. To achieve these objectives, the package provided for the introduction of a single EU-wide cap in the ETS, the introduction of national emissions target for non-ETS sectors as well as national targets for renewable energy. The Europe 2020 economic strategy¹ stressed the need to reconcile sustainability and economic growth.

2.2 The Energy Union 2014-2019

On the eve of the Paris agreement,² the EU updated its climate commitments to strengthen its credibility and diplomatic position vis-à-vis other UNFCCC parties. In October 2014, the European Council agreed on a new Climate and Energy framework for 2030, which included a 40% cut in GHG emissions, a 27% renewable energy target – binding at the EU level – and a 27% energy efficiency target. The European Commission under the Presidency of J.C. Juncker (2014 – 2019) carried on the effort to place climate action at the core of the Energy Union.

¹ European Commission. A Strategy for smart, sustainable and inclusive growth. [\(See more\)](#)

² United Nations (2015), Paris Agreement. [\(See more\)](#)

The Clean Energy Package, originally proposed by the Commission in 2016 and finally approved in 2019, translated into legislation the Commissions' objectives. Notably, the package paved the way for a shift away from fossil fuels and a gradual transition towards a carbon neutral economy by updating the 2030 targets for renewables and energy efficiency, respectively to 32% and 32.5%.

In November 2018, the Commission set out its long-term vision for a climate neutral EU, in line with the Paris Agreement objectives, and outlined different pathways to achieve carbon neutrality by 2050. The climate neutrality discussion was taken up by the new Commission and formed the foundation for the EGD proposal.

2.3 The European Green Deal

The political process after the elections brought Ursula. v. der Leyen as Commission President (2019-2024). On December 2019 the European Commission adopted a communication³ on the European Green Deal where it was revealed that the EGD was not meant to be a goal in itself, but a means to achieve several objectives, such as, a climate neutral EU in 2050, the implementation of the United Nations 2030 agenda and the Sustainable Development Goals. Moreover, the EGD was also presented as the growth strategy of the European Union, consolidating the trend of decoupling economic growth and an increase in GHG emissions. The original communication included over 40 key strategic actions⁴ to be proposed during the next two years touching upon, among others, climate, energy, industry, mobility, agriculture, biodiversity, sustainability or air pollution.

Fit for 55: Even if it can be argued that most of the legislative proposals (including those that are included in the Fit for 55 package) are updates of existing legislation, such a massive legislative review has no precedence in the EU climate and energy history. It is meant to change European society in a period when the public debate on policy matters is stunted due to the response that governments have given to the COVID outbreak.

3. The EGD Structure and Developments

3.1 Initial proposition

The European Commission under Ursula von der Leyen took office in December 2019 and announced the super ambitious '**European Green Deal**'. Compared to earlier EC plans, some of the new milestones are:

- Climate neutrality by 2050, to be enshrined in a 'European Climate Law', up from the 40% to 'at least a 55% emissions' reduction 2030 target.
- 'Sustainable Europe Investment Plan' of €1 trillion for 2021-2030 including the Just Transition Mechanism, based on the Just Transition Fund.
- 'Carbon Border Adjustment Mechanism' to address trade impacts and avoid carbon leakage. A new element was, that CBAM was planned as an own resource to ensure financing of the Recovery Plan.
- A 'Farm to Fork' strategy.

Regarding the institutional architecture, The European Commission has recently designed a new one in order to facilitate the coordination among the Green Deal different policies and legislations as well as between its horizontal aspects.

One issue that is raising concerns is the significant levels of EU expenditures which are also unprecedented, and which is contested by some as it raises concerns with respect to the future financial stability of the EU.

³ European Commission 2019, Communication on the European Green Deal ([See more](#))

⁴ European Commission 2019, Communication on the European Green Deal, Annex ([See more](#))

3.2 COVID-19 Recovery adjustments

On July 2020, EU leaders agreed on an unprecedented recovery package combining a reinforced multiannual financial framework (€1 074.3 billion) with an extraordinary €750 billion recovery instrument under the name of Next Generation EU. EU leaders also agreed that 30% of the total expenditure would target climate related projects, positioning the EGD at the center of the recovery.⁵

In addition to the financial package, EU leaders agreed to significant changes in the own resources system and on a roadmap for the introduction of new own resources including one on non-recycled plastic packaging waste (2021), a border carbon adjustment mechanism, a digital levy, a revised proposal linked to the EU ETS (proposals in 2021 and introduction in 2023), a financial transaction tax, a financial contribution linked to the corporate sector or a new common corporate tax base (proposals in 2024 and introduction in 2026).

3.3. The 2030 climate target plan

On September 2020 the European Commission presented its 2030 Climate Target Plan⁶ which included a proposal for increasing the EU 2030 emissions reduction target to at least 55%⁷ making this target the EU's new Nationally Determined Contribution (NDC) under the Paris Agreement, ready for submission to the UNFCCC.

At the same time the European Commission published an accompanying Impact Assessment⁸ and an EU-wide Assessment of National Energy and Climate Plans⁹. The impact assessment mentioned that the EU Emissions Trading System (EU ETS) and the Effort Sharing Regulation, combined with the 32% renewable energy target and 32.5% energy efficiency target were projected to reduce emissions by around 45% by 2030, and that therefore amendments in the legislative framework were needed to adapt to the new ambition.

3.3.1. Agreement on the Climate Law

The EU Climate Law was proposed by the European Commission in March 2020 being not just a climate law, but as emblematic of the Europe its proponents would like to see emerging in the post-COVID-19 era. The Climate Law provides for some sense of long-term predictability in terms of both mitigation objectives and governance, but which needs to be balanced with the lack of flexibility that it also inserts in a dynamic international context which is still uncertain.

The EU institutions negotiators reached an agreement on the Climate Law on April 20, 2021, just a day ahead of the Leaders' Summit on climate convened by US President Biden. Some of the key points of the agreement are the following:

- Greenhouse Gas Emissions Reduction Target of at least 55% compared to 1990.
- Limit of 225 Mt of CO₂ the contribution of removals to the net target.
- Establishment of a European Scientific Advisory Board on Climate Change.
- Proposition of an intermediate climate target for 2040, if appropriate, at latest within six months after the first global stocktake carried out under the Paris Agreement.
- Publication of a projected indicative Union's greenhouse gas budget for the period 2030-2050.
- Indicative voluntary sectorial roadmaps towards achieving the Union's climate neutrality objective by 2050.

⁵ The Recovery and Resilience Facility (main instrument of NGEU) establishes that 37% of projects expenditure shall be devoted to climate.

⁶ European Commission (2020), communication stepping up Europe's 2030 climate ambition. ([See more](#))

⁷ European Commission (2020) amended proposal for a Regulation on the EU Climate Law. ([See more](#))

⁸ European Commission (2020), staff working document, impact assessment. Stepping up Europe's 2030 climate ambition. ([See more](#))

⁹ European Commission (2020), an EU-wide assessment of National Energy and Climate Plans. ([See more](#))

4. Substantive Elements: An Overview

4.1 CBAM

After the 2019 announcement of the European Green Deal, consultations began to prepare the proposal for a carbon border adjustment mechanism (CBAM), to be included in the “Fit for 55” legislative package expected in June 2021. As part of the official consultation process, the Inception Impact Assessment and the Public Consultations took place in 2020. Following this process, the European Commission is finalizing the Impact Assessment, which will accompany the proposal on July 14th.

The European Commission was initially considering four options for a CBAM design: 1) Import tax; 2) ETS extension; 3) Notional ETS with a separate pool of allowances; 4) Consumption tax (excise or VAT type). Currently, No. 3 was widely considered the preferred option.

After more than a year of discussions on the design options of the EU CBAM there are strategic choices to be made during the interservice consultations and make the final proposal from the European Commission. Why we chose CBAM as the central piece to the Fit for 55 package? What is the role of free allocation for the sectors participating in the mechanism?

Even if there is no change to the current system until 2025, there are concerns that other legislative pieces, namely the EU ETS, will be impacted. There is a visible pressure on the revenues, both on the generation as well as the spending side. The redistribution aspect in CBAM also impacts third countries as their exporters might bear some of the EU CBAM costs. CBAM auctioning, less free allocation – one issues is where is the coordination between these elements of legislative package taking place?

Among the red line issues that are in the spotlight of the discussions can be highlighted: indirect emissions and inclusion of scope 2 & 3 emissions, value chain coverage threshold or the inclusions of exports. One last issue is accommodating foreign climate action: allowing challenges of the default values that may underpin the CBAM, and possibly consideration of national exemptions.

4.2 ETS – breaking down elements of the upcoming review

The upcoming review of the EU ETS will have to make the EU ETS able to achieve reductions of around 63% in covered sectors compared to 2005, which would mean coherence with the -55% overall target. The EU ETS, which has so far contributed to some degree to the decarbonization of the power sector, will need to tackle industry emissions, which since 2013 (and at least 2018) have mostly stagnated and need to decrease by around 22% by 2030 vs 2005 levels according to the Commission’s plan.

In the next decade, the ETS will be increasingly asked to tackle emissions by the industrial sector. Its review will therefore have to reconcile the preservation of the EU industrial competitiveness with the enhancement of the climate ambitions of the Bloc.

Early unofficial documents would seem to indicate that a more ambitious linear reduction factor will be coupled with a rebase of the CAP – probably by 100Mt in 2023. Under this scenario, sectors covered by CBAM would not receive free allocation, although many observers point out that CBAM and free allocation can in fact coexist in a ‘complementary’ fashion.

Crucially, the Commission proposes that 100% of ETS allowances revenues are used for climate-related purposes by Member States, up from 50% today. Moreover, an additional 2% of the cap will be allocated to the Modernisation fund.

ETS extension

The Commission is considering the extension of the scope of the ETS to maritime transportation. It is possible that after a 2021-2025 phase-in period, shipping companies will have to surrender allowances for 100% of their verified emissions starting in 2026. A separate ETS – without free allocated allowances and with its own Cap and LRF may be created for road transport and buildings, with compliance obligations for covered entities starting in 2026. To mitigate concerns about the low-price elasticity of these sectors and the potentially very high EUA prices, a MSR will operate which will release additional allowances on the basis of the average price of allowances.

4.3. The EU sustainable finance agenda in the context of the EGD

Sustainable finance is already embedded in many international and European agreements, such as the Paris Agreement¹⁰ and the EGD. The EGD stresses the huge investment gap to reach the EU 2030 climate targets, and the importance to align all sources of finance towards sustainability. The European Commission (EC), via its EGD Investment Plan, plans also to: 1) mobilise EUR 1 trillion of sustainable investments over the next decade through the EU budget; 2) create an enabling framework for private investors and the public sector; 3) provide tailored support to public administrations and project promoters in identifying, structuring, and executing sustainable projects.

There are, however, serious concerns being raised by prestigious think tanks such as IFO as to the impact that the components of the sustainable finance package may have on the functioning of the EU as a market economy. Notably, regarding inconsistencies between the EU Taxonomy design and the core objectives of financial regulation (i.e.: stabilise the financial system, limiting the risk taking, supporting the efficient allocation of capital in the economy).

4.3.1. The first EU sustainable finance strategy: 3 objectives and 10 action points

The sustainable finance strategy, published in 2018, mainly focuses on establishing an enabling framework for the private sector. The strategy identified 3 strategic objectives to be reached to face the sustainable finance challenge: 1) reorienting capital flows towards sustainable investments; 2) managing financial risks stemming from climate change and environmental degradation; 3) fostering transparency and long-termism in financial and economic activity. To achieve all these objectives, the strategy identified 10 separate action points, which combine legislative¹¹ and non-legislative initiatives.

Regarding the section dedicated to reorienting capital flows towards sustainable investments, the EC identified 5 action points. The first one dedicated to the establishment of an EU classification system for sustainable activities (i.e. the EU Taxonomy). The EU Taxonomy Regulation entered into force in July 2020 and the performance criteria for qualifying as taxonomy-aligned are being defined via delegated acts (DA)¹². The second action point of the strategy is the creation of standards and labels for green financial products, mainly via the EU Green Bond Standard (EU GBS) Regulation proposal. The third action point aims at fostering investment in sustainable projects, with the intention to connect the sustainable finance frameworks and tools

¹⁰ Article 2.1 of the Paris Agreement reads: “Making finance flows consistent with a pathway towards low greenhouse gas emissions and climate resilient development”

¹¹ Both new measures and targeted amendments to existing rules

¹² The first EU Taxonomy delegated act (DA) was released in April 2021 and was dedicated to climate change mitigation & adaptation. Another DA will be released for the remaining 4 environmental objectives by the beginning of 2022, and a complementary one (dedicated to agriculture, nuclear and gas) will be released after summer 2021

with relevant EU funds. The fourth action point intends to incorporate sustainability when providing financial advice¹³ and the fifth to develop sustainability benchmarks for financial portfolios.¹⁴

Actions for reaching the second strategic objective (i.e.: better managing financial risks caused by environmental matters) includes: better integrating sustainability in ratings and market research; clarifying institutional investors' and asset managers' duties and incorporating sustainability in prudential requirements. To conclude, the last two action points of the strategy aims at fostering sustainable finance disclosure, transparency, and long-termism.

4.4. The EU renewed sustainable finance strategy

On top of all the developments under the general umbrella of the EC strategy released in 2018, a new strategy was published on 6 July 2021. Such new strategy intends to finance the transition of the real economy towards sustainability, finally recognizing the EU transition challenge¹⁵. Notably, by supporting the financing of certain economic activities contributing to reducing greenhouse gas emissions; extending the EU Taxonomy framework to recognise transition efforts; and extending sustainable finance standards and labels that support financing the transition to sustainability (i.e. not only deep "green" but also "transition" labels).

On top of the section dedicated to transition finance, the new strategy brings more consistently on board the global dimension, by promising ambitious cooperation on initiatives and standards. There is also a section with considerations of inclusiveness for SMEs and consumers, and one for supporting the ability of the financial and economic system to internalize material risks coming from environmental degradation when pricing assets, planning investments, and taking strategic decisions.

4.5. Hydrogen

Hydrogen is gaining tremendous momentum in the EU, where a policy framework has been put in place at both, Member State's and EU level. At an EU Level the European Commission adopted its hydrogen strategy on July 8th 2020. The Council of the EU¹⁶ and the European Parliament¹⁷ reacted to the strategy on December 2020 and May 2021 respectively. At a Member State level several EU countries have put forward national hydrogen strategies revealing different approaches to key issues of the discussions.¹⁸

The current EU hydrogen regulation and policy is scattered over gas, electricity, fuels, emissions, industry, transport, heating, and sustainable finance regulation. The "Fit for 55 Package" will undoubtedly contribute to shape the regulatory landscape for hydrogen, however, there is still a considerable level of uncertainty about where (in what pieces of legislation) and how, key discussion issues will be addressed. Moreover, it is still unclear how wide the regulatory flexibility for Member States will be. The following chart intends to map where key issues of the discussions, will be found in the Fit for 55 package and in other relevant upcoming pieces of legislation.

One important issue to highlight is the debate that is not taking place, on the balance in the development of the hydrogen economy between the role of markets and central regulatory tendencies. It is felt that markets are taking a secondary role and that this will impact the overall ethos of the EU economy.

¹³ On April 2021, the EC adopted six amending delegated acts ensuring that financial firms include sustainability in their procedures and their investment advice to clients

¹⁴ The Regulation on EU Climate Benchmarks applies since April 2020

¹⁵ With "transition challenge", ERCST intends the challenge that the EU economy is facing and will face in the coming decades to reach climate neutrality by 2050

¹⁶ Council Conclusions 2020 "Towards a hydrogen market for Europe" ([See more](#))

¹⁷ European Parliament non-legislative resolution on a European strategy for hydrogen ([See more](#))

¹⁸ The Oxford Institute for energy studies and ewi (2021), Contrasting European hydrogen pathways ([See more](#))

Production	<ul style="list-style-type: none"> ❖ Binding classification (production processes) ❖ Additionality criteria for renewable H2. ❖ Imports v. exports 	<ul style="list-style-type: none"> ❖ RED III for Renewable Hydrogen and Gas Package for low carbon EU Taxonomy ❖ Delegated act on additionality ❖ Member States, CBAM.
Demand	<ul style="list-style-type: none"> ❖ Hard to abate vs. other sectors ❖ Hydrogen purity ❖ Hydrogen scarcity 	<ul style="list-style-type: none"> ❖ RED III, Rev. Energy Efficiency Directive, Rev. ETS Directive ❖ Secondary legislation ❖ Rev. RED III, Rev. Gas Package, Rev. State Aid, EU Taxonomy.
Transportation	<ul style="list-style-type: none"> ❖ Pace for infrastructure development ❖ Blending ❖ Repurposing 	<ul style="list-style-type: none"> ❖ Rev. TEN-E, Rev. Gas Package, EU Taxonomy ❖ Rev. TEN-E, Rev. Gas Package, Rev. State Aid, EU Taxonomy ❖ Rev. TEN-E, Rev. Gas Package, Rev. State Aid, EU Taxonomy
Incentives	<ul style="list-style-type: none"> ❖ CCfD ❖ Demand mandates ❖ Tax rebates ❖ Sustainable Finance ❖ State AID ❖ Funding Mechanisms 	<ul style="list-style-type: none"> ❖ MSs Level, ETS Directive ❖ RED III and Rev. Gas Package ❖ MSs Level ❖ EU Taxonomy ❖ Rev. State Aid Guidelines and IPCIs ❖ ETS Modernization & Innovation Fund, RRF, JTF, Horizon Europe, CEF, EIB financing

4.6. Just Transition

EU Ambassadors on 16 December 2020, endorsed the provisional political agreement reached by the German Presidency of the Council and the European Parliament on the new €17.5 billion **Just Transition Fund (JTF)**. The JTF together with InvestEU just transition scheme and public sector loan facility¹⁹, also with the EIB providing low-interest loans constitute the three pillars of the **Just Transition Mechanism**. The overall sustainable investments will be supported by the InvestEU Advisory Hub, that intends to provide technical assistance for, e.g.: decarbonisation projects; economic diversification projects; social infrastructures, etc. Notably, the overall thematic focus will be on low carbon & climate resilient activities (e.g. RES, energy efficiency, energy & transport including gas infrastructure & district heating) and on projects directly benefiting transition regions (with transport or energy projects).

5. State of play Before the Fit for 55 publication

EGD Tracker	
Until Today	Fit for 55 Package 2021
<ul style="list-style-type: none"> ➤ Presentation of the EGD (11-12-2019) ➤ Presentation of the European Green Deal Investment Plan and the Just Transition Mechanism (15-01-2020) ➤ Proposal for a European Climate Law to ensure a climate neutral European Union by 2050 (04-03-2020) ➤ Adoption of the European Industrial Strategy (10-03-2020) ➤ Proposal of a Circular Economy Action Plan focusing on sustainable resource use (11-04-2020) ➤ Presentation of the "Farm to Fork Strategy" (20-05-2020) ➤ Presentation of the EU Biodiversity Strategy for 2030 (20-05-2020) ➤ Adoption of the EU strategies for energy system integration and hydrogen (08-07-2020) ➤ Presentation of the 2030 Climate Target Plan (17-09-2020) ➤ Chemical strategy for sustainability (14-10-2020) ➤ Methane Strategy (14-10-2020) ➤ Renovation Wave (14-10-2020) ➤ Offshore renewable energy (19-11-2020) ➤ European Climate Pact (09-12-2020) ➤ European Battery Alliance (10-12-2020) ➤ New European Bauhaus (18-01-2021) ➤ New EU Adaptation Strategy (24-02-2021) ➤ Organic Action Plan (25-03-2021) ➤ Zero pollution Action Plan (12-05-2021) ➤ Sustainable blue economy (17-05-2021) 	<ul style="list-style-type: none"> ➤ Revision of the EU Emissions Trading System (ETS), and ETS as own resource ➤ Carbon Border Adjustment Mechanism (CBAM) and a proposal for CBAM as own resource ➤ Effort Sharing Regulation (ESR) ➤ Revision of the Energy Tax Directive ➤ Amendment to the Renewable Energy Directive to implement the ambition of the new 2030 climate target (RED) ➤ Amendment of the Energy Efficiency Directive to implement the ambition of the new 2030 climate target (EED) ➤ Reducing methane emissions in the energy sector ➤ Revision of the Regulation on the inclusion of greenhouse gas emissions and removals from land use, land use change and forestry (LULUCF) ➤ Revision of the Directive on deployment of alternative fuels infrastructure ➤ Revision of the Regulation setting CO₂ emission performance standards for new passenger cars and for new light commercial vehicles ➤ Revision of the energy performance of Buildings Directive (EPBD) (Q4 2021) ➤ Revision of the Third Energy Package for gas

¹⁹ https://ec.europa.eu/commission/presscorner/detail/en/ip_21_1935