Key Takeaways from COP27

Global heads of state met in Sharm El-Sheikh in Egypt from 6 to 18 November 2022 at COP27, the United Nations climate summit, to discuss more ambitious action to tackle climate change. Not surprisingly, energy security, climate finance for developing nations and a "just transition" were at the top of the agenda for world leaders this year. The Matheson team followed the negotiations closely and, in this insight, we explore the key takeaways and what this means in practice.

The Sharm el-Sheikh Implementation Plan: "*not a moment of unqualified celebration*"

UN Secretary-General António Guterres observed that COP26 had been driven by two overriding themes: justice and ambition. In a historic first, delegates to the 27th UN Climate Conference agreed, in the early hours of Sunday, 20 November 2022, to create a "loss and damage" fund to assist countries suffering from the impact of the climate crisis. Three Irish government departments, led by Minister Eamon Ryan, were at the centre of drafting, crafting and negotiating the historic agreement. The result represents a significant step towards climate justice.

Despite this historic achievement, COP26's President, Alok Sharma, remarked at the closing plenary of COP27 that "this is not a moment of unqualified celebration." COP27 failed to demonstrate greater ambition across a number of different areas and, crucially, in relation to ending the use of fossil fuels. This insight describes the key debates at COP27 and where future developments might lie.

Loss and Damage Finance

The EU agreed to support a "loss and damage" fund, subject to certain conditions:

- that the donor base be broadened to include sectors such as aviation, shipping and the fossil fuel industry;
- that the most vulnerable developing countries are targeted for support; and
- that a robust agreement to reduce emissions be put in place.

These conditions were partly met and developing nations accepted the offer.

The passing of the Inflation Reduction Act in the US, as we have previously discussed here, in conjunction with support from other wealthy countries, generated further the momentum for an agreement in Egypt "to establish a fund for responding to loss and damage". A transitional committee will assess what funding is needed, where the money should come from and whether to expand the donor base to countries like China or Qatar. There will be a further reporting obligation at COP28.

Some of the funding is to come through "existing funding arrangements" like development banks or debt relief while more will come from "innovative sources", which could mean taxes on fossil fuels, aviation or shipping. The EU specified that support should only go to "vulnerable" countries which the transitional committee will define. Countries agreed on the establishment of an organisation called the Santiago Network which will provide technical assistance in averting, minimising and addressing loss and damage resulting from climate change.

Fossil Fuels

At last year's COP26, the presidency made a push to "keep 1.5°C alive", referring to the most ambitious temperature limit in the Paris Agreement. At least 23 countries made new commitments in Glasgow to phase out coal power, including five of the world's top 20 coal power-using countries. The text of the COP27 agreement does promote renewables but also "low-emission" energy. It is possible to interpret this as including gas, a fossil fuel which is less polluting when burned than coal, or fossil fuels with carbon capture and storage. It holds the Glasgow Pact line on 1.5°C and the treatment of coal, but does not go any further. While the agreement recognises that the 1.5°C target "*requires rapid, deep and sustained reductions in global greenhouse gas emissions reducing global net greenhouse gas emissions by 43% by 2030 relative to the 2019 level*", President Alok Sharma highlighted a number of omissions from the text of the agreement. In particular, the fact that emissions must peak before 2025 in order to keep this target, that there was no mention of a clear follow-through on the phasedown of coal or a clear commitment to phase out all fossil fuels and that the text in relation to energy was weakened. On balance, he concluded that "*...in Glasgow... the pulse of 1.5 degrees was weak*". Now, "*[u]nfortunately, it remains on life support*".

Proposed Reforms to the International Financial System

Prompted by Barbados' Prime Minister, Mia Mottley, during COP26, a conversation about moving trillions of dollars into green and climate-resilient investments has been gaining momentum. These proposed reforms to the international financial system are happening outside UN Climate Change. The International Energy Agency estimates that $4 trillion needs to be invested in renewable energy every year by 2030 to reach net zero emissions by 2050. Countries called on multilateral development banks (MDBs) and international financial institutions to scale up and simplify access to climate finance and ensure their activities contribute to increased climate ambition. However, Prime Minister Mottley's flagship proposal to use IMF relief, known as special drawing rights (SDRs), to fund carbon-cutting projects does not feature in the text of the agreement.

In recognition of the fact that financial systems must be reformed, in September 2022, Matheson hosted a very informative event on Financing Through the Lens of ESG which is available on our Knowledge Hub. We previously considered the corresponding legal instruments: the SFDR and the Taxonomy Regulations in November of 2021 and we provided an overview of the various issues arising relating to the completion and filing of the SFDR Level 2 pre-contractual disclosure templates in "SFDR Level 2: Are You Ready to File?" in October 2022. If you would like to see a recording of these discussions, please contact our Knowledge Insights team.

Climate Finance

Wealthy countries have not yet provided the $100 billion they promised to deliver by 2020 over a number of COP meetings to help developing countries cut emissions and cope with climate impacts. As Lord Nicholas Stern, Chair of the Grantham Research Institute on Climate Change and the Environment at the London School of Economics and Political Science, stated these "*...investments will [also] generate a new and attractive form of economic growth and development that is sustainable, resilient and inclusive. The plan is that investment will be made mainly by the private sector, but will not occur without strong policy and greatly increased flows of capital at* *affordable cost. That in turn will require a major expansion of external finance from a range of sources, including the World Bank and other multilateral development banks...*" Talks on a new collective climate finance goal for 2025 were slow.

The text agreed in Egypt says the new goal will "*take into account the needs and priorities of developing countries*".

Carbon Trading Rules

Article 6.4 of the Paris Agreement proposed a voluntary global carbon market to assist countries in implementing their Nationally Determined Contributions (NDCs). The finalised COP26 Paris Agreement Rulebook progressed the Article 6.4 mechanism by introducing Article 6.4 emissions reductions (A6.4ER), which represents a reduction of 1 tonne of CO2 or equivalent. Where an A6.4ER produced is authorised for use towards achievement of an NDC or for other international mitigation purposes (for example voluntary carbon markets), it will become an internationally transferred mitigation outcomes (ITMO) that can be traded between countries. The rules for the Supervisory Body for the Article 6 mechanism were also agreed at COP26 and the body was established with 12 members, including at least one member from the least developed countries and one member from small island developing States.

On the last day of COP27, a draft decision on the Article 6.4 mechanism was published but overall, little progress was made on the Article 6.4 mechanism at COP27.

Mitigation Work Programme

At COP26 in Glasgow, countries agreed to set up a "*work programme to urgently scale up mitigation ambition and implementation in this critical decade*". The emphasis in Sharm el-Sheikh was how to structure this work programme. The final disappointing compromise was that the process should be "*non-prescriptive, non-punitive, facilitative, respectful of national sovereignty and national circumstances*" and "*not result in new targets or goals*" and talks will continue to 2026.

Adaptation

Countries agreed to develop a framework to guide delivery of the overall goal and to track progress on adaptation. This will take into account countries' vulnerability and capacity to cope and consideration will be given to a range of themes including water, food, agriculture and poverty, and science-based indicators including metrics and targets. Countries "noted with serious concern" the gap between current levels of adaptation finance and what is needed to respond to climate impacts.

A technical body made recommendations on how to define "removals". Many of the options

involve untested or controversial processes and negotiators sent the recommendations back for further work. Regarding bilateral carbon trades between countries, the text allows governments to designate any information about the exchange as confidential.

Just Energy Transition

There was a recognition that the current global energy crisis underlines the need to rapidly transform energy systems, including accelerating renewable energy roll out. Two days before the start of the summit, South Africa published details of a $84 billion investment plan to transition from coal to clean energy. It outlined details of a $8.5 billion deal with wealthy countries. On the sidelines of the G20 leaders' summit in Bali, wealthy countries announced a similar $20 billion deal with Indonesia. The funds include both public and private finance contributions. Similar ambitions exist in relation to Vietnam with plans for an agreement before the end of the year.

The concept of "just transition" arguably crystallised during COP27 and countries also agreed that "just and equitable energy transition" must be based on national development priorities and include social protection and solidarity measures, such as providing retraining programmes and support for coal workers affected by the transition. A work programme on just transition was established and an annual ministerial roundtable will be convened as part of this process.

A Right to a Healthy Environment

The right to a clean, healthy and sustainable environment was inserted into the final outcome text. This reference to a UN resolution approved only in July is significant as it offers a more central role for health in climate frameworks. A particular proposal by the African Group of Negotiators to recognise the special needs and circumstances to tackle climate action was rejected.

Conclusion

While the agreement to set up a loss and damage fund is a landmark achievement for climate justice, in several other respects, COP27 did not fulfil its overall ambition. Echoing the remarks made by COP26's President, Alok Sharma, Mary Robinson, Chair of the Elders leaders group, reminded us that "*...none of this changes the fact that the world remains on the brink of climate catastrophe." "Progress made on mitigation since COP26 in Glasgow has been too slow. Climate action at COP27 shows we are on the cusp of a clean energy world, but only if G20 leaders live up to their responsibilities, keep their word, and strengthen their will. The onus is on them.*"

India's presidency of the G20 began on 1 December 2022 and its call for a phasing down of all fossil fuels is a positive starting point for COP28 discussions in Dubai.

If you have any questions on COP27 or any other ESG matters, please contact Garret Farrelly, Owen Collins or your usual Matheson contact.