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Methane Regulation

Impact on Importers and Equivalence Regime

EU – October 2024

Overview

This alert focuses on the European Union's Methane Regulation (Regulation (EU) 2024/1787) (Regulation) and its implications for importers and exporters of oil, gas and coal into the EU. Specifically, it examines the obligations imposed on importers within the EU and the associated reporting requirements for exporters from third countries. A key emphasis is placed on the equivalence system, which allows exporters to demonstrate compliance with the EU's methane emission obligations through equivalent regulatory frameworks in their respective jurisdictions.

The Regulation establishes a comprehensive legal framework for the measurement, reporting and verification (MRV) of methane emissions in the energy sector. It mandates mitigation measures to prevent methane emissions, such as detecting and repairing leaks, as well as limiting venting and flaring. In addition, the Regulation includes global monitoring mechanisms to ensure transparency regarding methane emissions from imports of oil, gas and coal into the EU. It entered into force on August 4, 2024, and is directly applicable in all EU Member States. Given that the majority of methane emissions linked to fossil energy consumed within the EU occur outside its borders, this regulation is groundbreaking, as it is the first to regulate methane emissions from imports, which is the primary focus of this alert.

Regulatory Obligations for Importers

The Regulation extends its scope beyond the EU's borders to address methane emissions resulting from oil, gas and coal products imported into the EU. Importers are subject to significant compliance obligations under the Regulation, effective from January 1, 2027.

- **New contracts** – For supply contracts concluded or renewed on or after August 4, 2024, importers must demonstrate that the MRV measures applied by the producer are equivalent to those required of EU operators under the Regulation.
- **Existing contracts** – For contracts signed before August 4, 2024, importers are required to make "all reasonable efforts" to ensure that equivalent MRV measures are in place, which may include amending the terms of such contracts. From January 1, 2027, importers must submit annual reports outlining their efforts to ensure compliance with the Regulation and provide justification for any failure to secure the necessary amendments to existing contracts.

Importantly, while the Regulation does not impose an outright ban on imports of oil, gas or coal that fail to meet the requirements, it introduces a system of penalties to be enforced by Member States. These penalties, which must be effective, proportionate and dissuasive, may include periodic penalty payments, confiscation of profits, public warnings or administrative fines. Administrative fines are capped at 20% of the relevant entity's annual turnover from the preceding year, providing a strong deterrent.

MRV Equivalence and Waiver Possibility for Exporting Companies

An essential feature of the Regulation for exporters is the possibility of demonstrating compliance through regulatory equivalence. Exporting companies from third countries can avoid direct compliance with EU MRV rules if their home country's MRV measures are recognized as equivalent by the EU.

Under Article 28(5) of the Regulation, the MRV measures of the producer's country must ensure methane emissions quantification and reporting at both the source and site level, similar to the standards set out in Article 12 (for crude oil and natural gas) and Article 20 (for coal). These measures must also include independent third-party verification equivalent to the requirements outlined in articles 8 and 9 of the Regulation.

Furthermore, Article 28(6) empowers the European Commission to establish, via an implementing act, the procedure and requirements for third countries to provide evidence of equivalence. The delegated act, referenced in Recital 73 of the Regulation, encourages engagement with third countries, taking into account geopolitical considerations and the EU's obligations under international law. Thus, while the technical requirements for equivalence are already specified, the delegated act will focus on the process for submitting evidence to demonstrate equivalence.

Geopolitical Implications

The Regulation will have significant geopolitical implications, particularly for major gas suppliers, such as the US, Algeria and Russia. While Russia has already reduced its gas deliveries to the EU following the 2022 invasion of Ukraine, other suppliers, including Algeria and the US, may face greater challenges due to higher methane emission rates in their supply chains. The Biden administration, which supports global methane reduction efforts alongside the EU, has welcomed the Regulation and implemented its own methane rules for oil companies.

After US elections, a Harris administration would maintain and possibly strengthen regulation of methane, while a Trump administration could seek to reduce methane regulations, as his administration did in 2020.

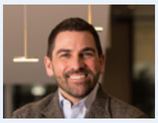
Concerns remain among industry groups that the EU may not recognize the methane standards of other jurisdictions as equivalent, potentially affecting the security of energy supplies. Other concerns relate the lack of practicability of the new rules to the production ecosystem in liquefied natural gas (LNG) producing countries, including the US. The European Commission is aware of these challenges and has indicated its pragmatism – whatever exactly that will entail is the subject of ongoing discussions with commission experts. It is important to note that the commission can only be pragmatic up to a point – any implementing act could be subject to legal challenge, for example by environmental NGOs, which is likely to deter the commission from a degree of pragmatism which might be vulnerable in the EU courts.

How We Can Help

Our team of EU regulatory lawyers and policy advisers is prepared to assist both importers and exporters in navigating the new requirements under the Regulation, and to seek a dialogue with EU lawmakers in order to find pragmatic solutions for the challenges the new EU law might create. We can advise on contract modifications to ensure compliance and mitigate the risk of penalties, but we can also help you in approaching EU decisionmakers with the right message, and at the right time.

Additionally, we can provide support in monitoring the drafting of the delegated act related to the equivalence mechanism, including organizing meetings with relevant technical units within the European Commission, as encouraged by Recital 73 of the Regulation. Our team can assist in ensuring that exporters from third countries can provide the necessary evidence of equivalence, ensuring compliance with the EU's legal framework while taking into account the specific regulatory mechanisms of their home countries.

Contacts



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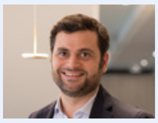

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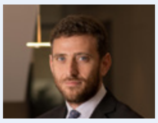

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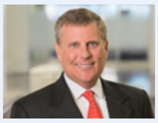

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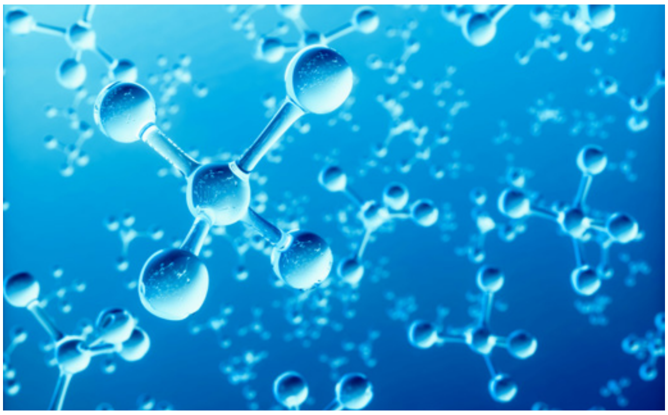

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