CADWALADER

January 24, 2023

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21 Attorneys General Write to Proxy Advisors ISS and Glass Lewis

January 24, 2023

Regulation

By Jason Halper
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On January 17, 21 Republican attorneys general **wrote** to proxy advisory firms Institutional Shareholder Services (ISS) and Glass Lewis over their recently released U.S. voting guidelines. As we **reported** last week, the updated guidelines include recommendations on a number of climate and social issues, including board oversight of and accountability for environmental and social issues, board diversity, racial equality audits, and disclosure of shareholder proposals. In their letter, the attorneys general claimed that the firms' "climate and diversity, equity, and inclusion priorities" may conflict with the contractual agreements they have with states' investment vehicles, including because these agreements "typically require that [the firms] consider only one goal: the economic value of the investments." By way of example, the letter cites Texas's Employees Retirement System proxy voting policy that requires proxy recommendations to "'consider only those factors that relate to the economic value of [the] investment' and be 'in accordance with the [plan's] economic best interest,' without subordination of the plan's interests 'to unrelated objectives' pertaining to social or environmental policy." The letter goes on to claim that the actions taken by ISS and Glass Lewis "may threaten the economic value of our states' and citizens' investments and pensions — interests that may not be subordinated to your social and environmental belief, or those of your other clients." In support thereof, the attorneys-general cite to the improbability of any of the top greenhouse gas emitters meeting the commitments of the Paris Agreement, and, therefore, "[a] rational company acting in the best interests of its shareholders would not voluntarily incur the massive expense estimated by the [International Energy Agency] pathway [to net zero]."

In response, an ISS spokesperson said that although the "letter reveals a fundamental misunderstanding of market forces at work," they would respond to the questions posed in the letter and continue to work towards its sole agenda of serving its clients.

As we discussed extensively in Cadwalader Climate, Republican lawmakers have opposed ESG-related developments in a variety of ways including **blacklisting from underwriting syndicates financial institutions that supposedly "boycott" energy companies**, **withdrawing funds from asset managers citing policy concerns**, and **launching investigations**. In a panel discussion on decarbonization at the World Economic Forum in Davos, Switzerland, **former Vice President Al Gore spoke** about the need to scale down "anti-climate finance" and in a recent interview, **CEO of BlackRock Laurence Fink stated** that the fund had lost approximately $4 billion in assets in 2022 due to the boycott of ESG (while adding that the firm added $230 billion in investments in the U.S. last year) and is seriously considering the criticisms it has received and working to "address the misconceptions."

Taking The Temperature: This letter is another development in the politicization of ESG-related policies governing investment decisions and company behavior more broadly. There is skepticism that consideration of climate issues ever run contrary to a fund's fiduciary or contractual duties of maximizing returns for shareholders given the likely materiality of such issues. It is clear, however, that certain states will continue to use the threat of "potential" breaches of fiduciary and contractual obligations (and corresponding investigatory authority) to exert political pressure over entities who have policies with which they disagree. On the other hand, investment firms and advisors maintain an obligation to consider risks that could undermine stockholder interest, including, for example, and as highlighted by ISS' response, climate change-driven economic shifts and changing market expectations in relation to social issues that could impact value.

Launch of National Blueprint for Transportation Decarbonization

January 24, 2023

Regulation

By Timbre Shriver
Associate | Global Litigation

On January 10, the Biden-Harris Administration released the **U.S. National Blueprint for Transportation Decarbonization: A Joint Strategy to Transform Transportation**, which is designed to cut all greenhouse emissions from the sector by 2050. The blueprint, developed by the Departments of Energy, Transportation, and Housing and Urban Development and the Environmental Protection Agency, provides a "framework of strategies and actions to remove all emissions from the transportation sector by 2050." According to the blueprint's **fact sheet**, the blueprint is meant to serve as a "guide for future policymaking and research, development, demonstration, and deployment in the public and private sectors." The **executive summary** of the blueprint provides that the agencies will "develop and implement the Action Plans and will work with other federal agencies, governments at the regional, state, local, and Tribal levels, philanthropic organizations, the private sector, and with global partners to achieve [its] milestones," which include research and investments to reduce greenhouse gas emissions before 2030 and scaling up deployment of clean solutions between 2030 and 2040.

According to the announcement, the U.S. transportation sector accounts for one third of all domestic greenhouse gas emissions and is the second-largest annual household expense in the U.S., both of which disproportionally impact disadvantaged communities. For these reasons, the blueprint is intended to facilitate a "well-planned transition to a decarbonized transportation system" to address these inequities and "provide equitable, affordable, and accessible options for moving people and goods," "create good-paying jobs across all segments of the transportation sector," and "strengthen America's energy independence." With respect to transportation decarbonization strategies in particular, the immediate impacts and long-term planning goals include increasing convenience "by supporting community design and . . . land-use planning at the local and regional levels," improving efficiency "by expanding affordable, accessible, efficient, and reliable options like public transportation and rail, and improving the efficiency of all vehicles," and transitioning to clean options "by deploying zero-emission vehicles and fuels for cars, commercial trucks, transit, boats, airplanes and more."

Taking The Temperature: The 88-page blueprint clearly sets out the current Administration's intentions with regards to improving the U.S. transportation sector by making it more accessible, affordable, and environmentally friendly. Specific areas that are expected to be subject to reform and regulation include public transportation, vehicle fuel economy, clean electricity, and hydrogen. However, the blueprint's framework remains fairly high-level, and the devil will be in the details. Policy goals will need to be translated into tangible projects in the real economy and will require significant investments in transportation infrastructure, which may require bipartisan

support that historically has been extraordinarily difficult to obtain. We will await any subsequent announcements with interest, but it is clear that the current administration is serious about making systemic changes in order to meet its decarbonization commitments.

Launch of Coalition of Trade Ministers on Finance

January 24, 2023

Regulation

By Sara Bussiere
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On January 19, it was **announced** at the World Economic Forum Annual Meeting in Davos, Switzerland that the European Commission, EU member states and 26 partner countries would launch a "Coalition of Trade Ministers on Climate." According to the press release, the coalition, which is the first ministerial-level global forum, will "foster global action to promote trade policies that can help address climate change through local and global initiatives" and seek to "identify the ways in which trade policy can contribute to addressing climate change." Trade ministers will "provide political guidance and identify trade-related strategies to adapt to changing climate conditions and extreme weather," such as, for example, the production and promotion of climate-friendly technologies. EU trade commissioner Valdis Dombrovskis **explained** that the creation of the coalition was "just the beginning" of international cooperation among finance ministers and other stakeholders "to become a truly global and inclusive platform for concrete actions and ideas."

The coalition is open to all interested countries, and is currently comprised of over 50 ministers from 27 jurisdictions. The four co-leads are Ecuador, the EU, Kenya, and New Zealand. The other participants are: Angola, Australia, Barbados, Cabo Verde, Canada, Colombia, Costa Rica, Iceland, Gambia, Japan (Foreign Affairs & Trade), Republic of Korea, Maldives, Mozambique, Norway, Philippines, Rwanda, Zambia, Singapore, Switzerland, Ukraine, United Kingdom, United States and Vanuatu.

The next meeting of the coalition will take place alongside the next World Trade Organization Ministerial Conference to be held in Abu Dhabi in the first quarter of 2024.

Taking The Temperature: This announcement reflects a continuation of recent announcements of multinational commitments such as the agreement on loss and damage concluded at COP27 and the Global Biodiversity Framework announced at COP15. While these bilateral commitments are notable, their significance will remain unclear until concrete action is taken to facilitate the change these coalitions seek to achieve. That being said, this coalition could have a significant impact on the environmental technology industry as trade ministers can help streamline and accelerate the trade of new products across the globe. Importantly, the coalition intends to carry out its operations in line with the United Nations Framework Convention on Climate Change alongside the Paris Agreement, which should help minimize any divergence of standards which undoubtably would increase costs and regulatory burden. It is unlikely, however, given that the next proposed meeting is not until 2024, that any change will take place soon.

Federal Reserve Announces Pilot Climate Scenario Analysis Exercise Details

January 24, 2023

By Daniel Meade
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Last week, the Federal Reserve Board (FRB) **announced** additional details on its pilot climate scenario analysis (CSA) involving six of the largest U.S. banks. The additional details include a **Participant Instructions Document** that calls for submissions by the participating banks by July 31, 2023. The FRB anticipates that it will publish insights and aggregate data from the exercise at the end of 2023. The FRB stated: "[t]his pilot CSA exercise will support the Board's responsibilities to ensure that supervised institutions are appropriately managing all material risks, including financial risks related to climate change."

As noted in the FRB's announcement, the "CSA exercise comprises two separate and independent modules: a physical risk module and a transition risk module. Physical risks represent the harm to people and property that may result from climate-related events, while transition risks represent stresses that may result from the transition to a lower carbon economy."

In the physical risk module, the FRB set a severe hurricane hitting the northeast of the United States as the common shock scenario. Each of the participating banks also were directed to selecct an idiosyncratic shock. The banks will apply those shocks to their Residential and commercial real estate loan portfolios and analyze the direct and indirect impacts of such a shock on those portfolios. In the transition risk module, the FRB instructed banks to consider "the impact on corporate loans and commercial real estate portfolios using a scenario based on current policies and one based on reaching net zero greenhouse gas emissions by 2050."

The FRB made clear that the "climate scenarios are neither forecasts nor policy prescriptions and do not necessarily represent the most likely future outcomes or a comprehensive set of possible outcomes." The FRB went on to highlight the difference between this exercise and regulatory stress tests, noting that the CSA exercise "is exploratory in nature and does not have consequences for bank capital or supervisory implications."

Taking the Temperature: Notwithstanding the additional details the FRB has provided on the CSA exercise, the Federal Reserve continues to emphasize that, as Chairman Powell said last week, the FRB is not a climate policymaker. Vice Chair of Supervision Michael Barr was quoted in the press release reiterating those sentiments, stating that "[t]he Fed has narrow, but important, responsibilities regarding climate-related financial risks – to ensure that banks understand and manage their material risks, including the financial risks from climate change. . . . The exercise we are launching today will advance the ability of supervisors and banks to analyze and manage emerging climate-related financial risks."