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ISSB Announces First Two Sustainability Disclosure Standards to Come Into Force from January 2024

February 28, 2023

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Following strong demand from investors for a timeline, the International Sustainability Standards Board (ISSB) has confirmed that draft IFRS S1 (General Requirements for Disclosure of Sustainability-Related Financial Information), and the draft IFRS S2 (Climate-Related Disclosures), will **become effective** in January 2024. The announcement follows a March 2022 consultation inviting **feedback** on the proposed standards.

Launched in November 2021, the ISSB is a standard-setting organization established by the International Financial Reporting Standards (IFRS) to promote common, consistent and reliable climate sustainability-related financial disclosures. The ISSB's aim with the standards is to provide "a comprehensive global baseline of sustainability disclosures designed to meet the information needs of investors in assessing enterprise value."

The ISSB also agreed to reference the European Sustainability Reporting Standards (ESRS) within the S1 appendix "as a source of guidance companies may consider, in the absence of a specific ISSB standard, to identify metrics and disclosures if they meet the information needs of investors." As we have **discussed**, the European Central Bank and European Banking Authority recently published their opinions on the first set of the ESRS. The ISSB highlighted the need to attempt to achieve consistency among the various major climate-related disclosure standards: "The ISSB announced with the European Commission and [the European Financial Reporting Advisory Group, which approved the ESRS in November] that they are working toward a shared objective to maximise interoperability of their standards and aligning on key climate disclosures." In this same vein, S1 and S2 themselves "build upon the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD) and incorporate **industry-based disclosure requirements** derived from SASB [Sustainability Accounting Standards Board] Standards."

Taking the Temperature: We have commented often on the challenges confronting issuers and investors with respect to climate-related disclosures, including challenges due to a lack of consensus on appropriate disclosures and a lack of quality data on which to base disclosures. The ISSB disclosure standards represent progress in the effort to unify globally climate-related reporting. As the IFRS commented in announcing the January 2024 effective date, "the decision on effective date is answering the strong

demand from investors for companies globally to disclose comprehensive, consistent and comparable sustainability-related information. IOSCO [the International Organization of Securities Commissions] and governments around the world, including G20 leaders and others, have been vocal about the urgent need for standards that enable companies to disclose information about sustainability-related risks and opportunities, starting with climate, to support systemic financial stability and for investor protection." We can expect additional standards covering disclosure of other sustainability topics, and, as Faber commented in Montreal, guidance on "adoption strategy, the support to adopt, the scalability, the capacity building, the proportionality… this is fully a part of what we need to deliver."

Yellen Calls on World Bank to Take Decisive Action on Climate Change

February 28, 2023

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On February 9, 2023, Treasury Secretary Janet Yellen **spoke** at the Center for Strategic and International Studies, urging the World Bank to "evolve" and be "bolder and more imaginative" in its operational approach to tackling global challenges such as climate change. She proposed that the World Bank "expand its vision" to include addressing these global challenges. According to Secretary Yellen, the problem lies in multilateral development banks' (MDBs') "core model," which involves countries borrowing to make specific investments aimed at addressing development constraints in their own countries. That model is insufficient to meet the moment. Such a model will always underinvest in addressing global challenges – since the benefits of investments in global challenges stretch far beyond the borders of the country where a given project takes place." As a result, the Secretary contended that the World Bank and other MDBs urgently needed to change, given declining progress in their "core mission of poverty reduction and inclusive economic growth."

Yellen referenced a **2022 G20 report** on development banks' capital adequacy frameworks, explaining that it provided a "solid blueprint" for the World Bank to "boost its financial capacity by responsibly stretching its existing financial resources." She highlighted several "promising ideas for exploration," which included the increased securitization of private sector portfolios and piloting the issuance of subordinated debt instruments. She also requested that the World bank identify "concessional resources available to countries to tackle global challenges," explaining that these resources could "incentivize the decommissioning of coal plants and protect displaced workers during a clean energy transition."

A spokesperson for the World Bank responded to Yellen's remarks, stating that the lender appreciates support from the U.S. and other shareholders "for finding ways to ramp up development finance to meet global challenges such as climate change, fragility, and pandemics. We see this support as a recognition by the global community of the World Bank's longstanding responsiveness and effectiveness, and we always welcome new ideas."

Notably, on February 23, 2023, President Biden nominated former Mastercard, Inc. CEO, Ajay Banga, to be the **next World Bank president**. President Biden stated that Banga is "uniquely equipped to lead the World Bank at this critical moment in history" and highlighted Banga's "critical experience mobilizing public-private resources to tackle the most urgent challenges of our time, including climate change." Yellen also publicly offered her support of Banga.

Taking the Temperature: Secretary Yellen's speech clearly reflects a view that the World Bank should be more aggressive in addressing various global challenges, including climate change. Her public backing of Banga's nomination supports her view, which makes sense given the massive investment required to transition to a green economy. While inherently uncertain, The World Economic Forum has estimated that it will require approximately $3.5 trillion more spending per year in order to achieve net zero by 2050 (and that does not take into account addressing harm already caused by climate change). Equally difficult is the question of which countries should pay. At the mitigation-focused COP27 in November in Egypt, the almost 200 countries in attendance reached an agreement to establish a dedicated fund to assist developing countries respond to loss and damage caused by climate change. "Loss and damage" refers to the concept that wealthier nations, which have been the largest emitters of greenhouse gas emissions, should compensate developing nations for harm caused by climate change. Likewise, at the COP15 biodiversity conference in Montreal in December, the main area of contention involved how to pay the costs that will be incurred to realize the Global Biodiversity Framework's (GBF) goals. The parties ultimately agreed to establish a global biodiversity fund with contributions of $20 billion/year by 2025 and $30 billion/year by 2030, from the existing United Nations Global Environmental Facility (GEF). The GBF also included pledges to cease at least $500 billion a year of subsidies for activities deemed harmful to nature such as agriculture and fishing. And, it bears mention that the World Bank has not been absent in terms of support for climate-related efforts. The Bank, along with other MDBs, is among the largest sources of funding for developing countries. In a statement released at COP27, the MDBs stated that in 2021 they "delivered $51 billion in Low and Middle Income Countries, of which $33 billion (65%) was for mitigation and $18 billion (35%) for adaptation; and $31 billion in High Income Countries, of which 95% was for mitigation and 5% for adaptation. In addition $41 billion of private finance was mobilised in parallel."

State Legislative Developments: Florida Goes One Way – Arizona, Indiana, North Dakota and Wyoming Go The Other

February 28, 2023

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On February 13, 2023, Florida Governor Ron DeSantis (R) **announced** his support for what his office described as "comprehensive legislation to protect Floridians from the woke environmental, social, and corporate governance (ESG) movement that continues to proliferate throughout the financial sector." Among other things, the **bill (HB 3)** would prohibit (1) fund managers working with state and local governments from considering ESG factors when making investment decisions; (2) state and local governments from using ESG factors when issuing bonds; and (3) "all state and local entities, including direct support organizations, from considering, giving preference to, or requesting information about ESG as part of the procurement and contracting process." The bill requires consideration of "only pecuniary factors," which are defined as those factors "expected to have a material effect on the risk or returns of an investment based on appropriate investment horizons consistent with applicable investment objectives and funding policy." Expressly excluded as permissible is "the consideration or furtherance of any social, political, or ideological interests."

On the same day, in an act that that reverses the practice of the prior administration, Arizona Attorney General Kris Mayes (D) **announced** that "Arizona would stop participating in investigations into major American banks and other financial institutions over ESG practices related to investing." Mayes explained "[c]orporations increasingly realize that investing in sustainability is both good for our country, our environment, and public health and good for their bottom lines."

Earlier this month, the Indiana Chamber of Commerce expressed a similar sentiment when it **announced** its opposition to a bill (HB 1008) that would prohibit public pension funds from investing in "funds or companies with policies of limiting investment based upon," among other things, "failure to meet or commit to environmental standards" or "work in the fossil fuels" industry. The Chamber described the bill as "anti-free market," indicating that it failed to take into account the "best interests of state pensioners." In support of its position, the Chamber cited a report from the Legislative Services Agency that estimated the bill would reduce returns for pensioners by nearly $7 billion over the next ten years.

In a similar vein, on February 1, 2023 the North Dakota House of Representatives **rejected** an "anti-ESG" bill by a 90-3 vote. The bill, **HB 1347**, would have required the state treasurer to

prepare, publicly post, and maintain a list of financial institutions that, without a business purpose, are "engaged in a boycott of energy companies." A "boycott of energy companies" was defined as "without a reasonable business purpose, refusal to deal with a company, termination of business activities with a company, or another action intended to penalize, inflict economic harm on, or limit commercial relations with a company because the company" engages in various activities in the fossil fuel industry or does business with such companies. The rejected bill was similar to laws that were enacted in various other states, including **Kentucky**, Texas and West Virginia.

Continuing the trend, on February 22, the Appropriations Committee of Wyoming's House of Representatives voted 7-0 to recommend that the House not pass two similar "anti-ESG" bills. One bill **(SF01721)**, like the bill opposed by Indiana's Chamber of Commerce, would have required managers of state funds to consider only "financial" factors, a term defined explicitly to exclude consideration of "social, political or ideological interests," including various environmental concerns. The other bill **(SF0159)** would deny government contracts to companies that "engage in economic boycotts," a term broadly defined to include "taking any commercial action that is intended to penalize, inflict economic harm on, limit commercial relations with or change or limit the activities of a company" based on the company's failure to satisfy defined environmental or other policy-based criteria.

Taking the Temperature: As we have discussed previously, the debate over the extent to which financial institutions may appropriately consider facts that fall under the rubric of "ESG" contains a deeply partisan element, and the developments in Florida, Arizona and elsewhere highlight that divide. The Florida bill, which is likely to become law given the Republican supermajorities in the state House of Representatives and Senate, is just another step in a series of moves by state Republican officials opposed to the consideration of ESG factors in investment decisions and upset over perceived insufficient support of the fossil fuels industry. On the other side of the ledger, Mayes's announcement in Arizona puts her in line with seventeen Democratic state attorneys general who wrote a letter late last year in support of investment managers being able to appropriately consider climate-related issues in making investment decisions.

Although the partisan nature of the ESG debate is likely to persist, the developments in Indiana, North Dakota, and Wyoming are noteworthy for their divergence from the overall tendencies of state Republican and Democratic officials toward ESG. The Indiana Chamber of Commerce, while technically a nonpartisan organization, wields considerable political influence in a state where Republicans control the governorship and both chambers of the legislature. Indeed the Chamber of Commerce's political action committee boasts that nearly 90% of the candidates it endorsed since 1990 won their races. The Chamber's strong disapproval of the Indiana legislation therefore is noteworthy given its otherwise traditional support of Republican candidates. Likewise, the Legislative Assembly in North Dakota is also controlled by Republicans, who by a 90-3 vote nonetheless rejected the type of financial institution blacklist bill that has become law in other Republican-controlled states; and Wyoming's House Appropriations Committee voted unanimously against two "anti-ESG" bills despite being comprised of six Republicans, including the chair, and just one Democrat. In our view, corporations and financial institutions will benefit from the depoliticization of ESG so that they can freely determine the underlying factors and criteria that are material to

(for a board) governance and management of the company or (for an asset manager) investment decisions and analysis.

European Commission Approves €515 Million in State Aid from Spain and Germany to Build Hydrogen-Powered Steel Plants

February 28, 2023

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On February 17, 2023, the European Commission granted approval for the Spanish and German governments to subsidize the construction of two renewable hydrogen-powered steel production facilities for Europe's largest steelmaker. Spain will **provide €460 million** to ArcelorMittal España to assist with replacing its blast furnaces at a facility in Gijón, where it operates two blast furnaces producing liquid hot metal from a mixture of iron ore, coke and limestone. The aid will support the construction of a renewable hydrogen-based direct reduced iron plant. Germany will **contribute €55 million** to ArcelorMittal Hamburg to build a "demonstration plant" for the production of green steel that will use 100% renewable hydrogen. It is expected that the facility in Spain will be operational by 2025 with the German project up and running a year later, in 2026. In both cases, the Commission found that the aid "has an 'incentive effect,' as the beneficiary would not carry out the investments in green steel production without the public support." Additionally, the Commission stated the aid would only have a "limited impact" on competition and trade within the EU and that it was necessary to "promote the production of green steel." If the projects net revenues end up being higher than anticipated, the companies will return a portion to the Spanish and German governments.

The Commission's press releases explain that the **2022 Guidelines on State aid for climate, environmental protection and energy (CEEAG)**, which came into force in January 2022, provide guidance on "how the Commission will assess the compatibility of aid measures for environmental protection, including climate protection, and energy which are subject to the notification requirement under Article 107(3)(c) TFEU [tax-exempt fuel users]." The Commission states that the aim of CEEAG is to "help Member States meet the EU's ambitious energy and climate targets at the least possible cost for taxpayers and without undue distortions of competition in the Single Market."

This announcement has been met with some resistance, including from the Institute for Energy Economics and Financial Analysis (IEEFA), which **accuses** the steelmaker of operating on parallel high and low carbon paths in different parts of the world. The IEEFA drew attention to ArcelorMittal's plan to develop two new blast furnaces in India, stating that the "plans for more coal-based steelmaking in India contrasts markedly with its developments in Europe and Canada." The report explains that "ArcelorMittal appears to be planning a two-speed decarbonisation with hydrogen-ready DRI [direct reduced iron] technology to be installed

overwhelmingly in developed nations, while the developing Global South is on the slower pathway involving more coal-consuming blast furnaces and as yet unproven CCUS [carbon capture, usage and storage] technology under its ‘Smart Carbon’ decarbonisation pathway.” A spokesperson for ArcelorMittal responded to the IEEFA’s report by stating that “the reality today is that neither green hydrogen nor carbon capture and storage are anywhere near ready for deployment at scale – that is why steel is recognised as hard to abate. But, unlike IEEFA , we do not take the view here in 2023 that they may never be. It is easy to dismiss the importance of the right political environment to incentivise the acceleration of decarbonisation – but the recently announced Inflation Reduction Act in the US has focused the world’s attention on how big a difference this can make.”

Margrethe Vestager, Executive Vice-President in charge of competition policy at the Commission, stated that the “€460 million measure enables Spain to support ArcelorMittal’s plan to decarbonise its steel production processes. It will contribute to the greening of a very energy-intensive sector, in line with our commitment to transition to a net zero economy. At the same time, the measure ensures that competition in the Single Market is not unduly distorted.” In respect of the German state aid, she said the “€55 million measure is an important step towards a more sustainable steel industry in Germany and the EU. By using renewable hydrogen, the green steel plant will contribute to reducing emissions in an energy-intensive sector and provide valuable insights for scaling up this technology across the EU. Today’s decision supports the EU’s transition to a net zero economy in line with the European Green Deal objectives.”

Taking The Temperature: It is worth considering this development in conjunction with U.S. Treasury Secretary Yellen’s recent speech (discussed in an accompanying piece today), where she called on the World Bank to be “bolder and more imaginative” in its approach to tackling global challenges such as climate change. Addressing the impacts of climate change and paying for the transition to a net zero economy will require trillions of dollars of funding annually. The EU’s support for Germany and Spain’s initiatives reflects a recognition that governments or government-supported institutions need to participate in that effort while also taking into account the potential for anti-competitive impacts as a result of such support. Also noteworthy is ArcelorMittal’s differing approaches in India and Europe, relying on carbon capture and storage in the former region while building green facilities in the latter. The company’s observation that its divergent approaches are in part attributable to greater government support in Europe underscores the challenges confronting poorer nations and companies that conduct business there in addressing climate-related impacts and timely making a green transition.