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Connecting Climate Change and the Law

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Investor Group Launches Plan to Boost Corporate Climate Engagement

May 5, 2023

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The Institutional Investors Group on Climate Change (IIGCC), a European membership body for investor collaboration on climate change, **announced the launch** of its **Net Zero Engagement Initiative (NZEI)**. A primary goal of the initiative is to "support investors align more of their investment portfolio with the goals of the Paris Agreement" while also increasing the number of companies subject to investor engagement on climate change. While **Climate Action 100+**, of which IIGCC is a coordinating member, "has transformed the scale and prominence of climate engagement with 166 high emitting focus companies, many more companies need to be engaged to align portfolios with net zero," said IIGCC.

As of the end of March 2023, **93 investors** have agreed to participate in NZEI, including Allianz, BNP Paribas, the Church of England Pensions Board, and Schroders. **107 companies** across a wide range of industries have **received letters** requesting confirmation that the companies have developed, or intend to develop, a net zero transition plan, which "provides a key tool for understanding the alignment of investment portfolios." The letters state that the "plans should set out both a company's emissions targets and a strategy for how it intends to deliver them. Recognising that most companies will not be able achieve net zero by themselves, they should also set out how they intend to support the transition more broadly."

The letters articulate the investment predicate for the NZEI as "recognising the financial risk presented by climate change and future regulatory risks posed by the failure of companies to prepare for economic transition." As a result, according to the letters, "many investors have committed to work towards aligning portfolios with net zero emissions through initiatives such as Paris Aligned Asset Owners and Net Zero Asset Managers Initiative. To date, more than 350 investors across these two initiatives, with over $60 trillion in assets under management, have committed to working towards achieving net zero emissions across their portfolios."

The letters recommend the adoption of four key plan components that align with the **Net Zero Investment Framework** corporate criteria:

1. a comprehensive net zero commitment by 2050 or sooner, "covering all relevant business areas and all material greenhouse gas (GHG) emissions scopes (1, 2 and 3);"

2. short-, medium- and long-term GHG targets “aligned with the relevant emission pathway and consistent with limiting the global temperature increase to 1.5 degrees Celsius;”
3. emissions performance disclosure specifying Scopes 1, 2 and 3; and
4. a credible decarbonization strategy which should include “the principal actions that you will take to deliver the GHG emissions targets including setting out capital expenditure plans and investment in climate solutions where relevant.”

To support the requests for confirmation, on March 15 IIGCC **published a guide**, “Investor Expectations of Corporate Transition Plans: From A to Zero,” which provides information on assessing transition plans, the rationale behind the requests and guidance on how companies can meet the requests.

Taking the Temperature: By expanding beyond the companies engaged by Climate Action 100+ the IIGCC is attempting to assist investors align a greater percentage of their portfolios with benchmarks consistent with the Paris Agreement’s goals. The IIGCC is aligned with commitments made by other net zero-focused industry groups such as the Paris Aligned Asset Owners (PAAO) and Net Zero Asset Managers (NZAM). While investor-led corporate engagement on climate appears robust, these initiatives also have been subject to controversy and challenges. As we reported in December 2022, Vanguard, one of the “Big Three” asset managers (along with Blackrock and State Street), withdrew from membership in NZAM. This withdrawal followed criticism from the Minority Staff of the U.S. Senate Committee on Banking, Housing and Urban Affairs over the “liberal views” toward ESG of the “Big Three” asset managers. Relatedly, Munich Re, Zurich and Hannover Re, three major insurance providers, announced their exit from the Net-Zero Insurance Alliance in the span of one month between March and April 2023, at least one citing antitrust risk as a motivating factor.

As for Climate Action 100+, we recently discussed its announcement of Benchmark 2.0, an assessment tool to evaluate the efforts of 166 focus companies to achieve a net zero transition relative to three objectives: taking action to reduce emissions; implementing strong corporate governance and accountability around climate-related risk; and enhancing climate-related financial disclosures. The organization also was the target of scrutiny from Congress, as we reported on a letter written by Republican members on the House Committee on the Judiciary to the steering committee members of Climate Action 100+ claiming that the investor-led initiative created “seems to work like a cartel.” House Republicans said they launched an investigation “probing whether major climate groups that spearhead the [ESG] movement are violating antitrust laws.”

Net zero transition plans also have exposed companies to scrutiny. We recently reported on a study finding that only 5% of FTSE 100 companies have disclosed credible and sufficiently detailed transition plans to become net zero by 2050; our report and other posts also commented on shareholder pressure for companies to adopt, disclose and meet net zero transition targets. At the same time, there is increasing shareholder and regulatory attention being paid to whether companies that have disclosed net zero plans are on target to meet those goals, exposing these companies to potential greenwashing challenges.

International Sustainability Standards Board Prioritizes Climate Disclosures

May 5, 2023

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The International Sustainability Standards Board (ISSB) **has approved a plan** that would implement a **transition period** for companies applying IFRS S1 (General Requirements for Disclosure of Sustainability-Related Financial Information), and IFRS S2 (Climate-Related Disclosures). Under the transition relief, companies would only need to report on climate-related risks and opportunities for the first year in which the ISSB Standards become effective. Companies would then be required to disclose other sustainability risks and opportunities beginning in the second year that the standards are effective. According to the ISSB, "this one-year transition relief would not change the effective date of IFRS S1. The ISSB tentatively decided in February 2023 to require that IFRS S1 be effective for annual reporting periods beginning on or after 1 January 2024. However, for an entity applying this transition relief in the first year it applies IFRS S1, the requirements in IFRS S1 would apply only insofar as they relate to the disclosure of climate-related financial information."

ISSB is a standard-setting organization established in 2021 by the International Financial Reporting Standards (IFRS). The IFRS' **goal** was to "develop—in the public interest—a comprehensive global baseline of high-quality sustainability disclosure standards to meet investors' information needs."

This transition program allows for companies to focus efforts on initially providing climate-related disclosures – what investors have "indicted [is] . . . the most urgent" disclosure – while also becoming familiar with the disclosure requirements under ISSB. Companies can use this first year to design and implement necessary reporting and disclosure systems without the full burden of all ISSB disclosure requirements.

During the transition year, companies would be exempt from: (1) reporting sustainability risks and opportunities other than for climate-related information; (2) providing annual sustainability-related disclosure at the same time as the related financial statements; (3) disclosing requisite comparative information; (4) reporting Scope 3 GHG emissions; and (5) utilizing the Green House Gas Protocol to track and measure emissions, so long as the company is currently using a different emissions measurement methodology.

The ISSB cautioned that "companies will still need to apply S1 in the first year they use the ISSB Standards to meet general disclosure requirements where they relate to climate. For example, S1 sets out the approach to materiality and requirements for connectivity of information with that in the financial statements, which are relevant to the disclosure of climate-related information."

Taking The Temperature: As we have commented before in discussing the ISSB standards, there remains an absence of consensus on an appropriate climate-related disclosure scheme and an ongoing lack of quality data on which to base such disclosures. In announcing the transition plan, Emmanuel Faber, Chair of the ISSB, commented that "[t]his transitional relief ensures companies can phase in their approach, initially focusing on the quality of the climate-related information they provide." By prioritizing climate-related disclosures over other sustainability-related reporting, the ISSB recognized that climate-related risks and opportunities are of paramount concern to investors.

European Commission Launches Consultation on EU Climate Targets for 2040

May 5, 2023

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The European Commission has launched a **public consultation** and a **call for evidence** seeking opinions on the EU's intermediary climate targets for 2040. This is a scheduled step in the EU's ambition to reach net-zero emissions by 2050 and part of a planned legislative agenda under the European Green Deal and the European Climate Law. The consultation is open to the public and has the stated aim of creating a "predictable environment to guide citizens, investment, and political decisions" towards a climate-neutral and sustainable future, and to ensure that Europe is resilient to climate change while harnessing the opportunities presented by the green transition.

Background

In 2019, the **European Green Deal** launched a comprehensive legislative agenda designed to put Europe on a path towards carbon neutrality. The adoption of the **European Climate Law** in 2021 made the EU's target of reaching net-zero emissions by 2050 legally binding, as well as the 2030 target of cutting emissions by at least 55%.

Article 4 of the European Climate Law requires the European Commission to make a legislative proposal for EU-wide 2040 climate targets within six months of the Global Stocktake under the Paris Agreement set for November 2023. Established under Article 14 of the Paris Agreement, the Global Stocktake is designed to "to assess the collective progress towards achieving the purpose of [the Paris] Agreement and its long-term goals," as opposed to progress on an individual country level, and will conclude at COP28 in December 2023. The 2040 climate targets likely will be set by amending the European Climate Law. As part of this process, the Commission will also publish a report on the projected indicative greenhouse gas budget for 2030-2050.

Consultation

The Commission will now collect the views of key stakeholders through a 12-week consultation ending in June. The **public consultation** is split into two sections: a general section and an expert section. A factual summary report and a synopsis report summarizing the results will be made public after the consultation. The Commission's final assessment will also take into account the advice of the European Scientific Advisory Board set up under the European

Climate Law. EU Member States and the European Parliament will ultimately decide on the EU's 2040 climate target.

Taking the temperature: The timing of the discussions for the 2040 EU climate targets is closely linked to the Paris Agreement's five-year "ambition cycle," which calls for parties to the agreement to reflect on the next target in the context of the UN process, with a view to communicate them ahead of COP29 in 2025. The European Commission is increasingly taking a proactive approach in aligning with the goal of carbon neutrality by 2050. As we previously reported, in Q1 2023, the European Commission imposed stricter emissions targets through the adoption of a carbon sinks goal, launched the Green Deal Industrial Plan and proposed reforms to the EU electricity market. Other countries also are taking steps towards carbon neutrality. Recent examples include initiatives in the UK, Canada, Singapore, and by the ASEAN Taxonomy Board to develop green taxonomies in order to facilitate renewable energy investment and finance transition activities.

ECB Issues First Reports on Climate Impact of Portfolios

May 5, 2023

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The European Central Bank (ECB) has **published** its first climate-related financial disclosures. The disclosures provide information on ECB portfolios, including detailing their carbon footprints and exposure to climate risks, and also discuss climate-linked governance and risk management. The disclosures are part of a Eurosystem-wide effort to increase transparency around the sustainability characteristics of European central bank portfolios.

The ECB issued the disclosures through two reports. A **report** on "Climate-related financial disclosures of the Eurosystem's corporate sector holdings for monetary policy purposes" covers corporate securities purchased for monetary policy purposes under the corporate sector purchase program (CSPP) and the pandemic emergency purchase programme (PEPP). An **additional report** on "Climate-related financial disclosures of the ECB's non-monetary policy portfolios" provides "quantitative and qualitative climate-related information about the ECB's own funds and staff pension fund. The information covers governance, strategy, risk management, and metrics and targets." The reports seek to provide greater transparency into the Eurosystem's follow-through on its climate obligations over time, charting decarbonization efforts against benchmarks in the Paris Agreement and reporting on the results of the ECB's **effort to "tilt"** its securities purchases toward companies "with a better climate performance."

According to the ECB, with respect to its corporate securities portfolio, even though "the portfolios' absolute greenhouse gas emissions have increased in recent years because the Eurosystem has purchased more securities for monetary policy purposes, issuers' carbon intensity has gradually declined. This is partly due to the fact that the companies in our portfolio have lowered their emissions for every million euro of revenue they earn, reflecting their efforts to significantly reduce their emissions and boost carbon efficiency." The ECB also attributes progress on the climate-related aspects of its portfolio to its **October 2022 decision** to incorporate climate change into ECB's monetary policy operations by favoring or "tilting" toward issuers with improved climate performance.

The ECB has also made efforts to transition its own funds portfolio. "The ECB has more than halved emissions from corporate and equity investments in its staff pension fund since 2019," and the "share of green bonds in its funds portfolio went from 1% in 2019 to 13% in 2022."

The ECB will now publish annual updates on climate progress related to these portfolios, increasing the detail of the disclosures as data quality improves. Eventually, the ECB plans to

disclose climate progress on its other monetary policy portfolios, including those under the public sector purchase programme (PSPP), the third covered bond purchase programme (CBPP3) and any other assets under the PEPP. The ECB will set its own interim decarbonization targets for its own funds portfolio, and will consider setting targets for corporate sector portfolios.

Taking the Temperature: The ECB has been active with respect to climate-related financial stability issues as well as attempting to promote green transition efforts through its monetary policies and issuer engagement. Among other things, along with the European Banking Authority, the ECB recently commented on "the first set of European Sustainability Reporting Standards, which provide guidance for companies performing environmental materiality assessments and disclosures of certain sustainability metrics; published "new experimental and analytical indicators" that are intended to help analyze climate-related risks in the finance sector and monitor green transition; undertook a thematic review into climate-related and environmental risks confronting 186 banks with total combined assets of €25 trillion; and, along with the European Supervisory Authorities, published a Joint Statement on climate-related disclosure for structured finance products. Notwithstanding these efforts, at least one member of the ECB's Executive Board has made the case that current climate-related actions being taken by the ECB will be insufficient for the central bank to meet its objectives of carbon neutrality by 2050, and urged more aggressive action.