UK Financial Regulator Proposes Reporting Template to Enhance Transparency of Shareholder Voting

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Amid ongoing scrutiny over proxy voting (particularly in relation to ESG-related resolutions), the UK's financial regulator, the Financial Conduct Authority, has launched a consultation aimed at developing a vote-reporting template for asset managers. In a June 2023 **consultation and discussion paper**, the FCA's Vote Reporting Group detailed its proposal for a "voluntary, standardized and comprehensive vote-reporting template" designed to facilitate communication and promote transparency from asset managers about their voting activity. The stated objectives of the framework include giving asset owners access to more consistent and comparable data for their own timely and accurate decision making, as well as increasing reporting efficiency for asset managers themselves.

Established as an independent working group by the FCA in November 2022, the Vote Reporting Group comprises diverse stakeholders, including members representing insurers, investment consultants and managers, NGOs, pension funds and proxy advisers, with the FCA serving as the secretariat. BlackRock, State Street, the UK Sustainable Investment Finance Association, pensions administrator Railpen, and asset manager Legal & General Investment Management (LGIM), as well as NGO ShareAction and the UN-supported investor network Principles for Responsible Investment, are among the group's members. The group's **purpose** is to develop proposals for improving shareholder vote reporting by asset managers operating in the UK, including a robust and standardized framework developed for and by industry.

The FCA asserts that increasing transparency and standardizing reporting requirements around vote-reporting will enable greater accountability and ultimately, deliver long-term, sustainable value for investors. With a standardized framework, according to the Vote Reporting Group, investors can benefit from useful data points that they can use to provide support for, or to question, the businesses in which they invest. Similarly, greater transparency around voting enables investors to choose asset managers whose stewardship reflects their values.

The proposed framework would require asset managers to report on company recommendations and their instructions for each vote, as well as explain in narrative form the reasoning and context behind the vote, and how the vote fits in with their overall voting policy. The information would be required for all shareholder resolutions, including environmental and social proposals, in cases where the asset manager rejects or abstains from non-sustainability-

related resolutions, and to votes relating to major decisions such as changes in company strategy, M&A or other special business. In putting together these reporting requirements, the Vote Reporting Group noted—and sought to balance—concerns from industry related to legal and compliance sign-off on voting rationales, as well as disclosure costs, with the benefits of standardized disclosure.

Public consultation of the proposed reporting framework runs through September 21, 2023.

Taking the Temperature: The Vote Reporting Group's consultation and discussion paper reflects a growing trend we have commented on toward shareholder engagement in connection with climate change, sustainability and other ESG-related issues. In the UK, for example, we recently reported on UK pension schemes threatening to vote against chairs of oil companies allegedly failing to meet climate pledges. In this year's AGMs, however, shareholder support for environmental and social proposals, including from the world's largest three asset managers, fell to the lowest in nearly six years. Although it is difficult to identify a single reason for this development, relentless resistance to ESG investing on the part of "anti-ESG" state and federal officials could be a factor (we have discussed this on several occasions and provide a detailed summary here).

In a related trend, certain U.S.-based asset managers have rolled out initiatives to permit beneficial owners greater say in how their investments are voted. We reported at the end of last year that Vanguard was implementing a program to offer "a number of proxy voting policy options for individual investors" in several of its equity funds. Blackrock's program permits institutional clients invested in certain funds in the U.S., U.K., Ireland and Canada to, among other options, "apply their preferred voting policy, meaning the client has either one that they have designed themselves or has chosen a third-party policy, in a consistent way across a broader share of their overall portfolio allocation."

For the most part, the push for greater transparency in vote reporting on the part of asset managers is in line with broader climate trends in the UK. The FCA has stepped up its Green Finance Strategy. The UK Pensions Regulator also has launched a new initiative to tighten regulation around ESG data published by trustees. As with asset managers, the Pension Regulator's underlying regulatory concern (as discussed previously) is that climate change reporting is left intentionally vague. The push from the FCA is somewhat at odds with a further delay to the introduction of its widely-anticipated Sustainability Disclosure Requirements which, having originally anticipated being published during H1 2023, are now expected to be published in Q3 2023.

Survey Finds More Executives' Compensation Tied to ESG Goals, But Progress Slow in Reaching Them

September 12, 2023

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A new study by the IBM Institute for Business Value found that approximately half of CEOs and their executive teams surveyed have their compensation tied to the organizations' performance in relation to sustainability goals. This figure represents a significant increase from just 15% reported in last year's study.

The annual study, **"CEO decision-making in the age of AI: Act with intention"**, released on June 27, 2023, also found that company decision-makers often fall short in reaching their organizations' ESG goals. While 95% of respondents have operational ESG goals, only 10% have made significant progress toward meeting them. Environmental sustainability has also fallen on the list of top organizational priorities from third last year to fifth this year, the report found. Meanwhile, "productivity or profitability" leaped to the top spot this year from sixth place last year. In addition, less than half—approximately 45%— of CEOs surveyed also reported having confidence in the ability to accurately report on ESG strategy and initiatives, due to the expanding definition of "sustainability" and uncertainty around the appropriate metrics to use.

The survey results are based on interviews with 3,000 CEOs from more than 30 countries and 24 industries, conducted by the IBM Institute for Business Value in cooperation with Oxford Economics. The interviews focused on executive perspectives on leadership and CEO decision-making regarding organizational challenges and opportunities, technology, data and metrics, and visions for a future shaped by generative artificial intelligence, **according to an IBM statement**.

Taking the Temperature: The IBM survey's findings on companies' lack of confidence in sustainability reporting are in line with the results of a study we reported on earlier this year by PwC and the Leadership Institute at the London Business School, which addressed the prevalence and efficacy of linking executive pay to ESG-related goals or targets. The report revealed that the vast majority of 50 of the largest European listed companies surveyed had adopted some form of carbon target incentive in executive pay, and an even higher percentage met their targets. However, the measures that companies most commonly failed to meet included the transparency of targets, which were rarely prospectively disclosed, and their quantitative link to the company's stated long-term carbon reduction goals, which were often unclear.

Investors are increasingly attempting to exert pressure on companies to clarify and strengthen the link between executive pay and meeting sustainability goals. As we reported in June, the shareholder advocacy group Australasian Centre for Corporate Responsibility (ACCR), HSBC Global Asset Management (UK) Limited and Amundi Asset Management filed a shareholder resolution pressing Japanese power company Electric Power Development Co., Ltd., known as J-Power, to disclose in its annual reporting how remuneration is linked to progress toward emissions reduction targets. The investors considered a direct link between executive compensation and the achievement of those targets to be important to incentivize management performance and protect corporate value, according to the resolution.

Montana Court Finds State Environmental Policy Unconstitutional

September 12, 2023

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As we touched on last week, on August 14, the Montana First Judicial District Court, Lewis and Clark County, entered its Findings of Facts and Conclusions of Law in ***Held v. State of Montana, et al.*** striking down certain provisions of the Montana Environmental Policy Act (MEPA), which restricted Montana from incorporating the impact of greenhouse gas emissions or other forms of climate change in environmental reviews (the MEPA Limitation). Plaintiffs were sixteen youths who, at the time of filing the initial complaint, ranged in ages from two through eighteen and, among other requests for relief, sought declarations of law concerning their constitutional rights in Montana to a clean environment and that Montana's "aggregate actions to implement a fossil fuel-based energy system . . . are unconstitutional."

Article II of the Montana Constitution provides that all persons have the "right to a clean and healthful environment." **Article IX** provides that the "state and each person shall maintain and improve a clean and healthful environment in Montana for present and future generations" and charges the state legislature to "provide for the administration and enforcement of this duty" and "provide adequate remedies for the protection of the environmental life support system from degradation."

In *Held*, the court conducted an analysis of climate science and environmental projections, drawing on expert testimony it declared "informative and credible," to find that there is an "overwhelming scientific consensus that Earth is warming as a direct result of human GHG emissions, primarily from the burning of fossil fuels," that "carbon dioxide . . . is the GHG most responsible for trapping excess heat within Earth's atmosphere," and that "science is unequivocal that dangerous impacts to the climate are occurring due to human activities, primarily from the extraction and burning of fossil fuels." In sum, the court stated that "Montana is warming, and the rate of warming is increasing."

The court then went on to find that climate change harms children uniquely and more acutely than adults. In the court's assessment, children are "uniquely vulnerable to the consequences of climate change, which harms their physical and psychological health and safety, interferes with family and cultural foundations and integrity, and causes economic deprivations." The court grounded its view not only on the impact of environmental degradation on children through poor air quality and other physical forms of pollution and changing weather patterns, but also the

"stress and distress" caused by fears of a changing environment and loss of cultural landmarks and nature's wonders that "can impact their physical health."

By enacting the MEPA Limitation, the court found that Montana was responsible for harming plaintiffs. The court found that the state has been aware of the harmful dangers posed by climate change since at least the 1990s, yet its modern energy policy and the MEPA Limitation "constrain[] [Montana] from making fully informed decisions through their environmental analysis about the scope and scale of impacts to the environment." Additionally, the court highlighted how expert testimony and other factual evidence showed that Montana could replace 100% of its GHG emissions with clean and renewable energy by 2050, demonstrating that the continued use and promotion of fossil fuels was not factually supported as a necessity for its energy policy.

Based on its factual determinations, the court held that plaintiffs had successfully shown that the MEPA Limitation was directly connected with the promotion of fossil fuel generation, that eliminating the MEPA Limitation would provide plaintiffs with appropriate redress by allowing the state to consider the impact of approved projects on the climate and environment, and that, in sum, the MEPA Limitation did not pass a strict scrutiny analysis because the State failed to show a compelling governmental interest that was necessary to overcome plaintiffs' rights under Montana's constitution. Accordingly, the court found that defendants continued "act[ions] in accordance with the statute would be unconstitutional."

It is expected that the Montana Attorney General's office will appeal the decision.

Taking the Temperature: As we have previously reported, it is likely that the decision in *Held* will become part of the discussion around climate-related litigation across the United States. There are currently multiple climate-related matters pending in state courts across the country. At least two other states have similar constitutional provisions protecting individual rights to enjoy a clean environment: Massachusetts and Pennsylvania. And, overall, there is a general upward trend globally in climate litigation.

If courts prove to be receptive to climate-centered litigation in the United States, that may also prove to be a significant development in the anti- and pro-ESG partisan divide. As we have reported, Republicans in Congress have attempted to pass legislation that would restrict investment advisors' ability to consider ESG factors when acting in the "best interests" of clients. GOP Attorneys General have targeted certain large asset managers for their ESG practices. And there has been a growing movement to use non-legal strategies to challenge companies and investment firms that utilize ESG metrics and pursue ESG goals. Depending on future developments in Held and other climate-related litigation in the United States, the judicial system may prove to be an increasingly prominent arena for resolution of competing positions in this area in the U.S. than it has to date.

EU Commission Releases 2023 Strategic Foresight Report Focusing on Environmental and Social Well-Being Objectives

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In July 2023, the European Commission published its annual **Strategic Foresight Report (the Report)**, focusing on how sustainability and people's wellbeing can help to achieve President von der Leyen's **six priorities for the European Union**, referred to as the "Open Strategic Autonomy." The Open Strategic Autonomy is characterized by: a European Green Deal, a Europe fit for the digital age, an economy that works for people, a stronger Europe in the world, promoting the European way of life and a new push for European democracy. The Report identifies six critical social and economic challenges to its sustainability transition and ten ways to overcome those challenges.

The six challenges identified by the report are:

1. **The rise of geopolitics**, in particular a changing geopolitical landscape marked by the Russian war against Ukraine, China's changing economic and global focus, and the focus of the U.S. on its domestic and foreign policies, that will challenge international cooperation on global issues, including climate change and the transition away from fossil fuels and toward green energy.
2. **The need to transform the current economic model** to ensure its sustainability and the wellbeing of Europeans, detach economic growth from the use of natural resources (currently up to 75% of Eurozone businesses are highly dependent on natural resources) and transition to more sustainable production and consumption.
3. **The need for sufficient investment from the private sector**, in addition to public funding from Member States, to drive the transition toward sustainability.
4. **The growing demand for workers** with the necessary skills and technical training to help navigate both the green and digital transitions in the face of workforce shortages and competency gaps (an estimated 85% of EU firms today lack staff with the required competencies).
5. **Eroding social cohesion**, including growing income inequality and the disproportionate impact of climate change on the most vulnerable populations, as well as intergenerational tensions that threaten trust in governments and the viability of a green transition.
6. **Threats to democracy** resulting from the erosion of public trust in government and other public institutions in dealing with growing socio-economic issues, coupled with the rise of extremist, autocratic or populist movements.

The ten action steps to address the six challenges are:

1. Ensure a new social contract appropriate for a sustainable European economy, including encouraging Member States to develop “inclusive, high-quality social services” and renewed welfare policies.
2. Strengthen the EU “single market” framework to drive a resilient net-zero economy and achieve “open strategic autonomy” and Eurozone economic security.
3. Enhance the EU's offer globally, including by focusing on the connection between internal and external policies, and strengthening key global partnerships.
4. Support shifts in production and consumption to support sustainability, in particular by “decarbonizing and depolluting” the economy, including streamlining regulation to impact the production side, and encouraging sustainable and balanced lifestyles on the consumption side.
5. Foster a “Europe of Investment”—ensuring that the EU is and remains attractive for investments in the net-zero and sustainable economy—including by developing “an agile, fast and responsive framework” for boosting private investments and “ensuring a positive business environment.”
6. Make public budgets “fit for sustainability” by, among other efforts, adapting fiscal and tax policies.
7. Revamp policy and economic indicators to reflect sustainable and inclusive wellbeing, including developing and incorporating “beyond-GDP” metrics into EU policymaking to measure environmental and social impacts.
8. Make sustained efforts to increase labor market participation for all segments of the population, in particular underrepresented populations, with a focus on both education (including technical, sustainability, digital and entrepreneurial skills) and adapting workplaces and working conditions.
9. Strengthen the EU’s ability to defend democracy and promote citizen agency, including by developing mechanisms to counter dis- and misinformation, making social media platforms more accountable and supporting independent media.
10. Complement civil protection with “civil prevention,” which includes developing “strategic foresight and monitoring capacities” to ensure that the EU is able to anticipate potentially disastrous events, such as the COVID-19 pandemic and Russia’s war against Ukraine, and prepare for their impacts.

The Report is expected to inform the agenda at the upcoming European Council, which will be hosted by Spain in October 2023, and also contribute to the agenda at the Commission and EU Parliament’s co-organized European Strategy and Political Analysis System conference in November 2023.

Taking the Temperature: European Commission President Ursula von der Leyen has long been a vocal advocate for EU leadership in the green transition. The Report, which addresses a host of non-climate sustainability issues in addition to climate concerns, acknowledges the significant geopolitical and economic challenges inherent in the EU’s transition agenda.

As the Report reflects, the EU is considering its dependence on, and place among, dominant global economic players, including the U.S. (which the Report acknowledges is a strategic partner) and China. It is also contemplating its wider impact on

decarbonization and green energy, both in the Eurozone and on emerging and developing nations, in particular on countries in Africa, Latin America and Asia that have strong economic ties to China. Point two of the ten action points focuses on economic security with an inward focus on Member State economic cooperation, while action point 3 focuses on the EU as an appealing alternative to the U.S. and China for outside partners, and action points 5 and 6 speak to making the EU attractive for private sector green investment, in particular because of the concern over the high cost of the sustainability transition. The Commission proposes increased funding from both the public and private sectors to facilitate the transition.

Of particular note is the proposed adoption of more expansive "beyond-GDP" metrics that factor in environmental and health concerns to enable the measurement of progress toward sustainability. Action point 7 makes that suggestion explicit and the report provides an in-depth look at some options for these metrics, including a well-being-adjusted, "enhanced GDP" measurement that would include different quality-of-life factors (health, education and recreation), work-related factors (unpaid care and domestic work), socio-economic inequalities, costs of environmental damage (such as pollution and greenhouse gas (GHG) emissions) and natural resource exhaustion.

Australian Competition Regulator Releases Draft Guidance on Greenwashing

September 12, 2023

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In July 2023, the Australian Competition and Consumer Commission (ACCC) released **draft guidance** for businesses making environmental and sustainability claims (the Draft Greenwashing Guidance). The Draft Greenwashing Guidance establishes best practices under the Australian Consumer Law (ACL) setting out how businesses operating in Australian jurisdictions can avoid greenwashing.

The Draft Greenwashing Guidance comes as a result of the ACCC's **ongoing investigations** of businesses in several sectors, including an "internet sweep" conducted in late 2022 of nearly 250 companies' websites across the energy, household product, food, cosmetic and other industries, and **we previously have discussed** ACCC's efforts in this area. **The ACCC's report** following its internet sweep published in March 2023 indicated that roughly 57% of Australian companies made "concerning"—vague or unclear—environmental or sustainability claims.

The Draft Greenwashing Guidance identifies eight key principles for businesses to follow in order to avoid greenwashing and includes specific prohibitions, best practices and examples. These include:

1. **Accurate and truthful claims:** more than just being true and accurate, businesses should be aware that even factually correct information could be potentially misleading (a significant challenge for companies that **we have previously discussed**);
2. **Evidence:** businesses should attempt to ensure that their claims are verifiable, with independent and scientific evidence being the most credible. Such evidence should be accessible to consumers. Businesses should have and be able to show, reasonable grounds for making forward-looking statements;
3. **Concealing or omitting important information:** consumers cannot make informed decisions if they are not presented with all material information;
4. **Conditions or qualifications:** other factors that could affect the truthfulness and accuracy of a claim should be explained to the consumer;
5. **Broad and unqualified claims:** broad claims are more likely to mislead consumers than specific claims that are substantiated;

6. **Clear and easily comprehensible language:** given that consumers may not have industry-specific knowledge, the language used should be clear and easy to understand, avoiding the use of technical terms;
7. **Visual elements:** the use of any visual elements (e.g. green-colored packaging) can create the impression to a consumer that a product or service is sustainable, and should therefore be considered carefully; and
8. **Directness and openness about sustainability transition:** aspirational claims should be avoided unless the business has developed clear and actionable plans as to how those ambitions will be achieved.

The consultation seeks feedback on common difficulties businesses face in making environmental claims, as well as common difficulties consumer groups might face in understanding such claims. Survey questions focus on what information is necessary to make an informed purchasing decision, as well as on the utility of QR codes, websites and product labels for providing such information. Other questions focus on the relevance of certified trademarks to help consumers better understand a business' environmental and sustainability credentials. The consultation period ends September 15, 2023. The ACCC expects that the final guidance, once approved, will be updated periodically.

Taking the Temperature: In its March 2023 announcement reporting the results of the internet sweep, the ACCC made clear that greenwashing is an enforcement priority, stating that there are, already, "several active investigations underway across the packaging, consumer goods, food manufacturing and medical devices sectors" related to allegedly misleading environmental claims, and promised "more targeted assessments into businesses and claims identified through the sweep," and "enforcement action where it is appropriate." In particular, ACCC Deputy Chair Catriona Lowe advised: "Businesses using broad claims like 'environmentally friendly', 'green', or 'sustainable' are obliged to back up these claims through reliable scientific reports, transparent supply chain information, reputable third-party certification or other forms of evidence. Where we have concerns, we will be asking businesses to substantiate their claims." In announcing the guidance in July, the agency declared that it is prioritizing "consumer, product safety, fair-trading and competition concerns in relation to environmental and sustainability claims." The guidance also serves as a strong indicator of the general approach the ACCC will take in investigating whether sustainability claims run counter to the ACL, as well as to enforcement outcomes.

Greenwashing is a growing concern and is increasingly an enforcement priority in various jurisdictions. In the EU, the European Commission published the Green Claims Directive, a proposal aimed at combating greenwashing and misleading environmental claims. The Green Claims Directive followed the EU's own "sweep" in 2020 during which it concluded that nearly half of environmental claims examined may be false or deceptive. Pursuant to the Green Claims Directive, if implemented, operators would need to, among other things, ensure that the claim "relies on recognized scientific evidence and state of the art technical knowledge," considers "all significant aspects and impacts to assess the performance," demonstrates whether the claim is accurate for the whole product or only parts of it, provides information on whether the product performs better than "common practice," identifies any negative impacts resulting from positive product achievements, and reports greenhouse gas offsets. The proposals are

being reviewed by the EU Council and Parliament and the timeline for implementation is therefore yet to be determined.

Accurate climate reporting across all sectors is a priority of Australia's current government in other sectors, including, as we recently discussed, in the financial markets, where the country's primary regulator, the Australian Prudential Regulation Authority, is currently developing its own climate reporting standards. Further, as we observed here, both greenwashing and "greenhushing" (the practice of not reporting or underreporting ESG credentials or initiatives due to uncertainty around emerging reporting frameworks) are part of the Australian Securities and Investments Commission's (ASIC) ongoing scrutiny of climate-related risk disclosures and potentially misleading statements.