GIBSON DUNN

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GIBSON DUNN ENVIRONMENTAL, SOCIAL AND GOVERNANCE UPDATE (MARCH 2023)

To Our Clients and Friends:

We are pleased to provide you with Gibson Dunn's ESG monthly updates for March 2023. This month our update covers the following key developments.

I. International

1. PRI releases new report on stewardship practices across investment managers

The United Nations Principles for Responsible Investment ("PRI") released a report on stewardship practices amongst their investment manager signatories on March 17, 2023, resulting from the PRI's analysis of responses from 1,858 investment managers. As part of the report, the PRI has identified a number of key areas for development which include: (i) the development of detailed, public responsible investment policies, (ii) broader coverage across assets under management, asset classes and ESG issues, (iii) clear accountability and governance for implementing responsible investment, (iv) expansion of client reporting, including quantitative analysis relating to ESG performance, and (v) robust implementation of the recommendations of the Task Force on Climate-Related Financial Disclosures.

2. IASB initiates project to consider climate-related risks in financial statements and proposes amendments to classification requirements for financial assets with ESG features

The International Accounting Standards Board ("IASB") launched a project on March 20, 2023 aimed at exploring whether and how companies can provide better information about climate-related risks in their financial statements. In undertaking the project, the IASB will research the cause of stakeholders' concerns in respect of: (i) the inconsistent application of the International Financial Reporting Standards' Accounting Standards in relation to climate-related risks, and (ii) the disclosure of insufficient information in financial statements about climate-related risks. The project will include a consideration of the work of the International Sustainability Standards Board in respect of financial statements to ensure that any proposals are complementary to that work.

Separately, on March 21, 2023, the IASB also published an Exposure Draft proposing amendments to IFRS 9 (*Financial Instruments*) and related requirements in IFRS 7 (*Financial Instruments: Disclosures*) to include clarifications in respect of the assessment of contractual cash flow characteristics in financial assets containing ESG features. Comments on the Exposure Draft are to be received by July 19, 2023.

3. TNFD releases fourth and final beta framework

On March 28, 2023, the Taskforce on Nature-related Financial Disclosures ("TNFD") released its fourth and final beta framework for nature-related risk management and disclosure for market participants to identify, assess, respond to, and disclose their nature-related issues. In this final beta draft, the TNFD has outlined its approach to disclosure metrics proposing a three-tiered approach as to disclosure metrics for nature-related issues: (i) core global disclosure metrics (that cover all sectors), (ii) core sector-specific disclosure metrics, and (iii) additional disclosure metrics (that can be used more flexibly). The TNFD is expected to release its final recommendations in September 2023.

4. APLMA, LMA and LSTA publish two guidance documents on green, social and sustainability-linked loans

On March 3, 2023, the Asia Pacific Loan Market Association ("APLMA"), the Loan Market Association ("LMA") and the Loan Syndications and Trading Association ("LSTA") announced the joint publication of two new ESG guidance documents to support the development of green, social and sustainability-linked loans. The first of these documents entitled "Guidance for Green, Social, and Sustainability-Linked Loans External Reviews" is intended to provide best practice guidance on the professional and ethical standards for the external review process, which is recommended in certain circumstances by the Green Loan Principles, the Social Loan Principles or the Sustainability-Linked Loan Principles, in connection with entering into green, social, or sustainability-linked loans respectively. The second guidance document entitled "Guidance on Social Loan Principles" is designed to sit alongside the Social Loan Principles and is intended to provide greater clarity for market participants with regards to the requirements of the Social Loan Principles.

II. United Kingdom

1. UK government publishes an updated green finance strategy and a strategic framework for international climate and nature action

On March 30, 2023, the UK government published: (i) its revised green finance strategy (the "Strategy"), which is an update to its earlier 2019 predecessor, and (ii) its 2030 Strategic Framework For International Climate And Nature Action (the "Framework"), which sets out the direction for the UK's integrated approach to international action on nature and climate up to 2030. Both the Strategy and the Framework are important cogs in a series of mechanisms aimed at furthering the UK's goal to become the world's first "net-zero financial centre".

The Strategy showcases the UK government's focus on five key objectives: (i) the growth of the UK's financial services sector, (ii) investment in the green economy, (iii) financial stability to manage risks from climate change and nature loss, (iv) incorporation and adaptation of nature and climate into the government's green finance policy framework, and (v) alignment of global financial flows with climate and nature objectives.

On the other hand, the Framework sets out three key global goals to ensure that the UK delivers internationally on its climate and nature goals: (i) keeping the 1.5°C target within reach by halving global emissions, (ii) building resilience to current and future climate impacts, and (iii) halting and reversing global nature loss. It proposes to do so by focussing on six local objectives: (i) a transition to clean technologies and sustainable practices, (ii) building resilience and adapting to climate impacts, (iii) increasing protection, conservation and restoration of nature, (iv) the strengthening of international agreements and cooperation to accelerate the delivery of climate and nature commitments, (v) alignment of global financial flows with a net zero future, and (vi) shifting trade and investment rules and patters to support the transition to a climate and nature positive future.

2. UK Treasury publishes a consultation paper on a potential regime for ESG ratings providers

On March 30, 2023, the UK Treasury published a consultation paper on a potential regulatory regime for ESG ratings providers. In the consultation paper, the Treasury outlines that the proposed regime would broadly seek to establish a framework whereby any assessment (excluding raw ESG data collection) regarding one or more ESG factors, whether or not it is labelled as such, provided to a UK user in relation to a number of specified investments, would be deemed to be a restricted activity in the UK. Consequently, such restricted activity could only be carried out if the relevant person (individual or corporate) is either authorised by the appropriate regulator or exempt from the authorisation requirement. The consultation paper itself seeks market participants' views on a range of issues, such as whether there should be fewer requirements for smaller providers and the scope of the regulatory regime. The consultation will close on 30 June 2023.

3. FCA outlines areas for improvement for ESG benchmarks

On March 20, 2023, the UK's Financial Conduct Authority ("FCA") announced that it had completed a preliminary review on ESG benchmarks and reported that the overall quality of ESG-related disclosures made by benchmark administrators was poor. At the same time, the FCA announced that it had sent a further letter to benchmark administrators outlining the key issues it had identified, which included: (i) lack of sufficient detail on the relevant ESG factors considered in benchmark methodologies, (ii) lack of accessibility and clarity of the underlying methodologies for ESG data and rating products, and (iii) ESG benchmark administrators not fully implementing all ESG disclosure requirements.

4. UK Treasury Committee raises concerns on consumer cost of the FCA's proposed ESG designation criteria and the FCA publishes update on its proposals

Following the UK's Financial Conduct Authority's ("FCA") a consultation paper in October 2022 proposing new criteria that a UK investment fund would need to meet to describe itself as "sustainable" (or similar), on March 9, 2023 the Treasury Committee raised concerns with the FCA that consumers who have invested in investment funds guilty of greenwashing may have to pay to move their investments into other 'sustainable' funds. As a result, the Treasury Committee has called for the FCA to conduct a more detailed cost-benefit analysis of its proposals and provide an assessment of the risks to both consumers and the funds industry. The FCA subsequently published an update on its proposals on March 29, 2023, confirming that the regime would be aimed primarily at protecting consumers, that there will be flexibility as to the labelling restrictions, and that it will seek international coherence with other regimes. The FCA's full Policy Statement on the topic is expected to be published in Q3 of 2023.

III. Europe

1. EU Commission proposes reforms of the EU electricity market design to boost renewables

On March 14, 2023, the European Commission announced a proposal for a European Union ("EU") Regulation to reform the EU's electricity market which envisages revisions to several pieces of key EU electricity legislation, notably the Electricity Regulation, the Electricity Directive, and the REMIT Regulation. The key proposals include the introduction of: (i) measures to incentivise more stable longer term contracts with non-fossil power production, (ii) more clean flexible solutions to compete with gas, such as demand response and storage, and (iii) a wider choice of consumer contracts and clearer information about them to allow consumers to lock in secure, long-term prices to avoid excessive risks and volatility (while retaining the flexibility for consumers to enter into dynamic pricing contracts to take advantage of price variability to use electricity when it is cheaper).

2. EU Commission proposes the Net Zero Industry Act

On March 16, 2023, the European Commission proposed the Net Zero Industry Act, which aims to simplify the regulatory framework for the manufacturing of technologies (or key components of technologies) which are key to achieve climate neutrality. The Act supports in particular eight strategic net zero technologies: (i) solar photovoltaic and solar thermal technologies, (ii) onshore wind and offshore renewable energy, (iii) batteries and storage, (iv) heat pumps and geothermal energy, (v) electrolysers and fuel cells, (vi) biogas/biomethane, (vii) carbon capture and storage, and (viii) grid technologies (which also include electric vehicles' smart and fast charging). Other net zero technologies are also supported by the measures in the proposed Act, to a different degree, including sustainable alternative fuels technologies, advanced technologies to produce energy from nuclear processes with minimal waste from the fuel cycle, small modular reactors and related best-in-class fuels. The proposed Act now needs to be discussed and agreed by the European Parliament and the Council of the European Union before its adoption and entry into force.

3. EU Commission proposes a directive on "green claims"

The European Commission proposed the Green Claims Directive on March 22, 2023, which would have a significant impact on businesses making "green claims" for their products in the European Union. A "green claim" under the directive may include any message or representation in any form that states or implies a positive or no environmental impact for a product, service, or organisation. The directive, among others, provides for strict rules for evidence supporting any such green claims made by companies, mandates third-party verification for green claims, and requires businesses to provide consumers with information on such claims, either in a physical form or via weblink or QR code.

4. European Parliament and European Council reach a deal on cleaner maritime fuels

On March 23, 2023, the European Parliament and the European Council reached a provisional agreement to establish a fuel standard for ships to steer the European Union ("EU") maritime sector towards the uptake of renewable and low-carbon fuels and decarbonisation. This agreement is part of the EU's "Fit for 55" target of reducing net greenhouse gas emissions by at least 55% by 2030. The proposed legislation requires that the greenhouse gas intensity of fuels is lowered over time (below the 2020 levels of 91.16 grams of CO2 per MJ), initially by 2% as of 2025, increasing incrementally and reaching up to 80% reduction as of 2050.

IV. United States

1. Biden vetoes anti-ESG investment legislation

The president of the United States Joe Biden issued the first veto of his presidency on March 20, 2023, rejecting legislation that sought to void the Department of Labor's rule allowing fiduciaries to consider ESG factors when choosing retirement investments. This ESG legislation, which took effect on January 30, 2023, was finalised in November of last year, following an executive order signed by President Biden in May 2021 that directed federal agencies to consider policies to protect against the threats of climate-related financial risk. The rule has been subject to significant debate, with opponents arguing that it will hurt retirement savings but the Department of Labor has emphasised that the rule permits, but does not mandate, fiduciaries to consider these factors.

2. West Virginia House of Delegates passes bill targeting ESG shareholder votes

On March 28, 2023, the governor of West Virginia, Jim Justice, signed legislation that targets shareholder votes (on behalf of the state's investment boards) that factor in ESG principles. The West Virginia House Bill 2862 seeks to designate "*environmental, social, corporate governance, or other similarly oriented considerations*" as factors that should not be considered in shareholder votes cast by the state's Investment Management Board or the fund managers it entrusts with casting such votes, unless such ESG factors directly and materially affect the financial risk or financial returns of the relevant investments. This is expected to impact decisions on investments of over USD $4 billion as the West Virginia Investment Management Board is tasked with investing assets for the retirement systems of deputy sheriffs, emergency management services, judges, municipal police officers, firefighters, public employees, state police officers and teachers within the state.

3. Proxy Preview publishes 2023 report on ESG shareholder proposals

On March 7, 2023, *As You Sow,* the Sustainable Investments Institute, and Proxy Impact, published the Proxy Preview 2023 report, containing information on hundreds of shareholder proposals, including environmental, corporate political spending, human rights, diversity, sustainable governance issues and others. Key takeaways from the report regarding 2023 developments are: (i) a continued increase in climate change shareholder proposals, and (ii) a significant expansion of shareholder proposals on reproductive health, in response to the United States Supreme Court's decision from June 2022 that is prompting a wave of restrictions across the United States. Proxy Preview also reports a surge in proposals pressing companies to commit (or re-commit) to international standards that protect the right to organise unions, notes that corporate political influence proposals are evenly split among lobbying, election spending and values congruency, and predicts (based on early indications) that anti-ESG resolutions, which increased in numbers last year, will expand further.

4. **COSO releases new supplemental guidance on internal control over sustainability reporting**

On March 30, 2023, the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") released supplemental guidance for organisations on improving internal control over sustainability reporting ("ICSR"). The supplemental guidance uses the globally recognised COSO Internal Control Integrated Framework as its basis and includes the following notable aspects: (i) references to the role of the internal audit function in sustainability reporting in the scope of the guidance, reflecting their integral part of ICSR, (ii) key themes to consider as organisations continue their journeys toward establishing and maintaining an effective system of internal control over financial and sustainable business information, and (iii) insights from companies with a particular ICSR focus to help more firmly establish ICSR practice within the internal audit profession.

V. APAC

1. **Japan announces timeline for introducing sustainability disclosure standards**

Japan announced on March 2, 2023 that it plans to introduce its own sustainability disclosure standards based on the International Sustainability Standards Board ("ISSB") framework ahead of the 2025-2026 financial year. The timeline for this was announced following a meeting between the ISSB and the Sustainability Standards Board of Japan and includes a proposed initial draft of the standards to be tabled by March 31, 2024 and final form standards to be issued by March 31, 2025. It is expected that the standards will be voluntary initially, with mandatory requirements to follow at a later date (which is yet to be decided).

2. **Malaysia's stock exchange plans to introduce a sustainability reporting platform in April**

Bursa Malaysia announced on March 22, 2023 that it is set to launch a sustainability reporting platform in April, in conjunction with the London Stock Exchange. The platform is expected to serve as a repository where both listed entities and small-to-medium enterprises can calculate their supply chain carbon emission impact and disclose common ESG data in accordance with established global standards, such as those of the Task Force on Climate-Related Financial Disclosures. The announcement follows last year's memorandum of understanding between Bursa Malaysia and the London Stock Exchange, which seeks to improve collaboration between the two exchanges, in particular in relation to ESG educational initiatives, implementation of supply chain finance and corporate ESG reporting solutions.

3. South Korea reduces 2030 emission reduction targets for industrial sector

On March 21, 2023, the South Korean Presidential Commission on Carbon Neutrality and Green Growth announced via a press release from the Korean Ministry of Environment that it has decided to cut South Korea's 2030 targets for reducing gas emissions (compared to its 2018 levels) in the industrial sector by 3.1% from the 14.5% set in late 2021 to 11.4%. The announcement also notes that South Korea is committed to maintaining its national goal of cutting emissions by 40% of 2018 levels and the gap created by this reduction is expected to be filled by switching more energy sources to renewables and making more reductions overseas. The Commission has backed its proposal noting that it has been necessitated "*in light of realistic domestic conditions including raw material supply and technology prospects*."

Please let us know if there are topics that you would be interested in seeing covered in future editions of the monthly update.

Warmest regards,

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