GIBSON DUNN

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

To Our Clients and Friends:

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

I. International

1. ISSB proposing to give relief on Scope 3 emissions and certain other data points in first year of reporting against S1 and S2

The International Sustainability Standards Board (ISSB) is proposing to extend reliefs available to support companies applying the ISSB's first two Standards—S1 (general requirements) and S2 (climate).

The relief will enable companies to focus initial efforts on ensuring they meet investor information needs around climate change and means companies can prioritise putting in place reporting practices and structures to provide high-quality information about climate-related risks and opportunities in the first year of reporting using the ISSB Standards.

Companies will then need to provide full reporting on sustainability-related risks and opportunities, beyond climate, from the second year. This follows the view from investors that disclosures around climate-related risks and opportunities are the most urgent.

2. Launch of Venture Climate Alliance

The Venture Climate Alliance (VCA), an organization created by leading global venture capital firms to define, facilitate, and realize net zero-aligned pathways for early-stage investments, launched on April 25, 2023 with a goal to build a robust movement within the venture industry to combat climate change. CA members have committed to supporting a rapid, global transition to net zero or negative carbon emissions by 2050 or sooner, and will take specific, near-term steps to achieve this goal, both within their respective firms and in their roles as investors and advisors to their portfolio companies.

As one of the first institutional touchpoints between capital markets and early-stage innovation, venture capital investors have helped thousands of new companies from initial development to commercialization and scale. The VCA provides a forum through which member firms will develop best practices for collecting, interpreting and reporting carbon emissions, and climate impact data, as well as tools and guidance to help to overcome barriers associated with aligning early-stage investments with net zero goals.

3. G7 sets collective targets on renewable energy

The Group of Seven wealthy nations (G7) recently issued a Communique setting out ambitious collective goals to increase their solar power and offshore wind capacity. Their aim is to expedite the development of renewable energy and hasten the phase-out of fossil fuels. However, they did not endorse a 2030 deadline for ending the use of coal, instead leaving room for continued investment in gas. The members committed to boosting offshore wind capacity by 150 gigawatts and solar capacity by more than 1 terawatt by 2030. They also agreed to speed up the phase-out of fossil fuels without capturing CO2 emissions, with a target of achieving net-zero energy systems by 2050 at the latest. The G7 nations also pledged to take practical and timely measures to accelerate the phase-out of unabated coal power generation.

While Canada and some other G7 members support ending the use of unabated coal-fired power by 2030, others are still exploring ways to achieve that goal. The G7 countries acknowledged that renewable energy and energy security are compatible goals and committed to reaching a shared target for 2050. They also pledged to reduce additional plastic pollution to zero by 2040, ten years earlier than previously planned.

II. United Kingdom

1. Northern Ireland faces legal action over new gas storage project

Northern Ireland’s decision to sign off an undersea project that could provide a quarter of the UK’s gas storage capacity will be challenged in the High Court in Belfast over environmental concerns in an action brought by Friends of the Earth Northern Ireland and local campaign group No Gas Caverns. It is believed to be the first case of its kind where the courts have had to grapple with the implications of climate change in the context of government decisions.

A judicial review hearing will start in the week commencing 8 May 2023, where lawyers will argue that the Northern Ireland Department of Agriculture, Environment and Rural Affairs (DAERA) failed to properly consider the environmental implications of the project when granting permission for the Islandmagee Gas Storage development.

2. Financial Conduct Authority to lead first GFIN Greenwashing TechSprint

On 11 April 2023, the UK Financial Conduct Authority (FCA) announced that it would be leading the Global Financial Innovation Network (GFIN)’s first ever virtual Greenwashing TechSprint. The TechSprint will be hosted on the FCA’s Digital Sandbox and aims to bring together international regulators, firms and innovators to address sustainable finance as a collective priority. UK-based firms are invited to apply from 17 April 2023.

The GFIN is a group of over 80 international organisations committed to supporting financial innovation in the interest of consumers. The GFIN's Co-ordination Group, which sets the overall direction, strategy and annual work programme, is currently chaired by the FCA.

In light of the growing number of investment products marketed as 'green' or making wider sustainability claims, the FCA wishes to ensure consumers and firms can trust that products have the sustainability characteristics they claim to have. The objective of the TechSprint is to develop a tool or solution that can help regulators and the market effectively tackle the risks of greenwashing in financial services.

There are currently 13 international regulators that have signed up to participate in the TechSprint. The TechSprint will launch on 5 June 2023 and will run for 3 months, ending with a showcase day in September 2023.

3. The FCA's view of Green Mortgages

Green mortgages – a mortgage which includes an incentive for people to either purchase an energy efficient property or improve the energy efficiency of an existing property - have a growing role to play in decarbonising the UK's housing stock by helping borrowers to improve the energy efficiency of their homes. The incentives could be a discount to the fixed rate or a cash rebate after completion of agreed improvements.

In a recent speech by the FCA's Director of Retail Banking emphasised the role that lenders have in this endeavour and flagged the risk of them missing their decarbonisation targets if they don't evolve their support for homeowners to enhance energy efficiency. Brokers should see an increase in the availability of green mortgage products and innovation and they have a key role to play in helping borrowers navigate a complex and nuanced landscape in terms of green home finance.

Equally, there are certain risks in requiring lenders to make more green mortgages that could lead to greenwashing if the majority of loans are made to newer, and already efficient, homes or too much innovation such that the number of products available outstrips demand from consumers.

The FCA has also made it clear that lenders need to deliver products that are ethical, socially responsible and green and meet expectations of the consumers based on the advertising or marketing of the products.

III. Europe

1. EBA consultation on benchmarking of diversity practices and policies

On 24 April 2023, the European Banking Authority (EBA) published a consultation paper on draft guidelines on the benchmarking of diversity practices including diversity policies and gender pay gap under the Capital Requirements Directive IV (CRD IV) and the Investment Firms Directive (IFD), addressed to Member State competent authorities (NCAs).

The benchmarking of diversity practices will allow NCAs to monitor diversity trends over time, including the identification of common practices for diversity policies and information on the gender pay gap at the level of the management body. The aspects of diversity that will be analysed concern the gender, age, educational and professional background as well as the geographical provenance of members of the management bodies. The benchmarking of diversity practices should be based on a representative sample of institutions and investment firms.

The EBA will analyse the diversity practices, including diversity policies and the gender pay gap and publish a benchmarking report at the EU level, including a country-by-country analysis every three years. The data is not collected annually as the composition of the management bodies is not expected to change significantly in the short term, but should change in the longer term through taking appropriate measures within institutions and investment firms.

The EBA plans that the first data on the diversity practices under the guidelines should be reported in 2025 with a reference date of 31 December 2024, including in situations where the financial year differs from the calendar year.

2. European Council adopts new rules on pay transparency

The Council has adopted new rules to combat pay discrimination and help close the gender pay gap in the EU. Under the pay transparency directive, EU companies will be required to share information about how much they pay women and men for work of equal value, and take action if their gender pay gap exceeds 5%. Once in the role, workers will be entitled to ask their employers for information about average pay levels, broken down by sex, for categories of employees doing the same work or work of equal value. They will also have access to the criteria used to determine pay and career progression, which must be objective and gender neutral. The new directive also includes provisions on compensation for victims of pay discrimination and penalties, including fines, for employers who break the rules.

3. Parliament adopts new law to fight global deforestation

The European Parliament adopted a new EU law on 19 April 2023 that will ban imports deemed to be driving deforestation. The legislation, which has to get final approval from the European Union's member countries, would apply to coffee, cocoa, soy, timber, palm oil, cattle, printing paper and rubber, and derived products, coming from countries around the world.

Imports that come from land that was deforested after 31 December 2020 will be prohibited in the EU market. Companies sending such merchandise to Europe will have to show a certificate guaranteeing they do not come from such zones, with checks conducted on a sliding scale according to how high risk the exporting country is ranked. Companies will also have to verify that these products comply with relevant legislation of the country of production, including on human rights, and that the rights of affected indigenous people have been respected.

IV. United States

1. Biden Executive Order - environmental justice

On 21 April 2023, President Biden signed the executive order "Revitalising Our Nation's Commitment to Environmental Justice for All", charging all federal agencies with a duty to pursue environmental justice. The executive order directs federal agencies to thoroughly review environmental and health impacts on communities. Under the new requirements, federal agencies must notify communities if toxic substances are released and host public meetings to inform local residents of any resulting health risks.

Increasing concerns about environmental justice come in the wake of the East Palestine train derailment on 4 February 2023, which resulted in the uncontrolled release of hazardous materials into the surrounding area. Following this incident, the Biden-Harris administration has growingly focused on the disproportionate impact of climate change and pollution on lower-income and otherwise disadvantaged communities. This executive order seeks to reduce the burden on such communities by requiring federal agencies to assess the "cumulative impacts" of an area's environmental and health problems when making decisions on new facilities or projects.

Under the executive order, President Biden has established a new Office of Environmental Justice within the White House Council on Environmental Quality, which will oversee federal agencies' efforts on environmental justice. In conjunction with this, the White House Council on Environmental Quality will publish an Environmental Justice Scorecard monitoring federal agencies' progress.

2. Environmental Protection Agency announces proposal on new auto pollution limits

The Environmental Protection Agency (EPA) plans to release its most stringent new emission standards for cars and light trucks. Sources familiar with the matter indicate that the rules are intended to ensure that electric vehicles (EVs) make up 54% to 60% of all new cars sold in the US by 2030, and 64% to 67% by 2032. This aligns with the U.S. President Joe Biden's goal of EVs accounting for at least 50% of new vehicle sales by 2030.

The EPA's proposal follows California air regulators' vote last year to ban the sale of new gasoline-powered cars by 2035 and set interim targets for phasing out these cars. California aims to have 70% of zero-emissions vehicles in all new car sales by 2030, and other states are also planning to adopt California's rules, driving a shift to EVs. Unlike California's policy, which directly targets vehicle sales, the EPA intends to implement increasingly stringent greenhouse gas emissions rules for automakers to follow from 2027 to 2032, thus promoting the electrification of the industry. In addition, the US Treasury Department released new rules on April 18 that will provide federal tax credits of up to USD 7,500 to buyers of certain EVs.

3. DOE report on CO2 management in US and steps needed to achieve net zero commitments by 2050

On April 24, the Department of Energy published a new report on carbon management, as part of its ongoing series of Pathways to Commercial Liftoff Reports. In particular, the report indicates the United States will need to rapidly accelerate investment in hydrogen, nuclear and long-duration energy storage in order to meet its commitment to obtaining net-zero emission by 2050, from an approximate USD 40 billion to USD 300 billion by 2030. In addition, the report states that the United States will need to store c.400–1,800 million tonnes of CO2 annually.

V. APAC

1. HKSE consultation paper on enhancements to climate-related disclosures

On 14 April 2023, the Hong Kong Stock Exchange published a consultation paper on enhancements to its climate-related disclosures regime, aiming to achieve closer alignment with the International Sustainability Standards Board Climate Standard, expected to be published before the end of June 2023.

At present, Appendix 27 to the Hong Kong Stock Exchange Listing Rules requires companies to disclose climate-related information on a "comply or explain" basis; the proposed changes would mandate companies to make those disclosures. Listed companies would also be subject to additional climate-related disclosure obligations under the revised Appendix 27. These relate to governance, strategy, risk management, and metrics and targets. Of particular note, an issuer would be required to disclose any climate-related risks and opportunities identified; any strategies prepared in response to those climate-related risks and opportunities; how the business is placed to prepare for and respond to climate-related changes; and any current and anticipated financial effects of climate-related risks.

It is anticipated that the revised HKSE Listing Rules and Appendix 27 will come into effect on 1 January 2024, subject to the responses to the consultation, due by 14 July 2023.

2. New Australian vehicle fuel efficiency standard

Australia is set to introduce fuel efficiency standards as part of its new national electric vehicle (EV) strategy, in a bid to catch up with other developed economies in promoting EV adoption. According to Energy Minister Chris Bowen, the new standards will stipulate the amount of carbon dioxide a car could produce while running. Details of the new EV strategy will be finalized in the coming months The Department of Infrastructure, Transport, Regional Development and Communications published a consultation paper on 19 April 2023 . Australia's Electric Vehicle Council (EVC) has welcomed the move and stressed the need for strict standards, warning that Australia will "remain the world's dumping ground for dated high-emission vehicles."

Australia was the only developed country, aside from Russia, that did not have or was not setting fuel efficiency standards. The lag in environmental rules has made it difficult for EVs and low-emission cars to compete with dirtier and less efficient vehicles in Australia. In 2022, only 3.8% of cars sold in Australia were electric, while the proportion stood at 15% in the UK and 17% in Europe. Bowen acknowledged the need to boost the construction of EV charging facilities. As of December 2022, the country had only 4,900 public chargers at fewer than 2,400 sites. To address this, a policy requiring the installation of one fast charger every 150 kilometers on the highway will soon be implemented, according to Bowen, for the convenience of 83,000 EV drivers on Australian roads.

3. India extends waiver of transmission fees for green hydrogen plants

India will exempt transmission fees for renewable power used in hydrogen manufacturing plants built up before January 2031, extending a waiver previously available for projects set up before July 2025. According to sources familiar with the matter, the move will enable more green hydrogen projects to qualify for the 25-year waiver of transmission charges, thus reducing the manufacturing costs. A government official explained that large-scale hydrogen and ammonia projects will require three to four years to construct, which means that many of them may not come into operation by June 2025.

India aims to become the world’s cheapest producer of green hydrogen - hydrogen produced by splitting water using electricity from renewables. It plans to bring down the manufacturing cost from current levels of USD 4-5 per kg to between USD 1-1.5 per kg. According to industry estimates, renewable energy, including transmission, accounts for 65%-70% of the cost of producing green hydrogen. Therefore, the government official stated that every one rupee decrease in renewable energy costs would result in a 60 Indian rupee (USD 0.73) reduction in the cost of green hydrogen. The inter-state transmission charges range from 1-2 rupees per unit of power transmitted. Besides waiving transmission fees, the Indian government will provide green hydrogen fuel producers with incentives worth at least 10% of their costs, under a USD 2.11bn program called “Strategic Interventions for Green Hydrogen Transition (SIGHT) Program”. The scheme, effective June 2023, is intended to produce affordable green hydrogen and reduce greenhouse gas emissions.

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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