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Table of Contents:

- Investors Pressure European Banks to End Financing for New Oil and Gas Fields
- Launch of Financial Services Committee Republican ESG Working Group
- Aviva Outlines Stewardship Priorities for 2023
- French Financial Regulator Calls for Review of SFDR Minimum Standards

Investors Pressure European Banks to End Financing for New Oil and Gas Fields

February 24, 2023

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On February 7, a group of 30 investors, representing over $1.5 trillion of assets under management, wrote to the CEOs and board chairs of five major European banks "urging them to stop directly financing new oil and gas fields by the end of this year." The banks are: **Barclays**, **BNP Paribas**, **Crédit Agricole**, **Deutsche Bank** and **Société Générale**. According to the NGO ShareAction, which is coordinating the campaign, the banks are the largest European financiers of "top oil and gas expanders after HSBC over the period 2016 – 2021." Last December, HSBC announced an **updated** energy policy that included a commitment, among other things, not to "provide new finance, or new advisory services, to any client" for projects relating to (1) "new [oil and gas] fields where the final investment decision was made after December 31, 2021" or (2) "infrastructure whose primary use is in conjunction with new [oil and gas] fields." The letters, which are substantially identical, contend that "eleven out of twenty-five of the biggest European banks," including HSBC given its updated policy, "now have some form of asset financing restriction for new oil and gas, regardless of supply segment. This sets a new minimum level of ambition for all banks committed to net-zero by 2050." In its **press release**, ShareAction expressed the concern "that new oil & gas fields may jeopardize the global path to net-zero" and that "these activities were holding back the renewable energy revolution in Europe." The letters also urge the five banks to change their dealings with the energy companies in question: asset financing for new oil and gas has been found to represent only eight per cent of total financing to top oil and gas expanders. We therefore encourage banks to swiftly turn their attention to the companies behind these new oil and gas fields."

ShareAction has been active lately, **recently co-filing** a shareholder resolution seeking details of the "specific plan" for Glencore PLC, a multinational commodity trading and mining company, "to align thermal coal production with emissions reductions commitments." Last year, the NGO **published** a report concerning the biodiversity and climate strategies of the 25 largest European banks.

Taking the Temperature: This announcement is further evidence of a continuing trend of investors seeking to influence climate-related company policy. This is not just a European development, with similar announcements in the U.S. targeting financial institutions' climate transition plans, including finance emissions reductions targets. As

we have reported, increasing numbers of companies are publishing climate transition plans and should expect that these will be subject to shareholder or regulatory scrutiny.

Other recent climate-focused shareholder activity includes the recent announcement by environmental nonprofit ClientEarth that it has asserted what it claims is the first derivative action in the High Court of England and Wales against Shell plc's board of directors, accusing the directors of violating Sections 172 and 174 of the Companies Act. ClientEarth claims that Shell is not "properly managing climate risk" and therefore its board is in breach of its legal duty to act with reasonable care, skill and diligence. Court filings are not currently publicly available. The action against Shell follows another case brought by ClientEarth in Paris against Danone for allegedly violating France's Corporate Duty of Vigilance Law in that the company supposedly does not have an adequate plan to reduce its plastic footprint. Just yesterday, on February 23, three other NGOs – Oxfam France, Friends of the Earth France and Notre Affaire à Tous – sued BNP Paribas in the Paris Judicial Court for violating the Duty of Vigilance Law (the same law at issue in the suit against Danone) relating to the bank's fossil fuel financing activities. And, yet another NGO, Global Witness, recently filed a complaint with the Securities and Exchange Commission (SEC)'s Climate and ESG Task Force asking that it investigate Shell for possible violations of the federal securities laws relating to disclosure concerning its financial investments in renewable energy sources.

Launch of Financial Services Committee Republican ESG Working Group

February 24, 2023

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On February 3, the Chair of the House Financial Services Committee, Patrick McHenry, **announced** the establishment of a nine-person Republican ESG Working Group to "combat the threat to our capital markets posed by those on the far-left pushing environmental, social, and governance (ESG) proposals." The group is to be led by Oversight and Investigations Subcommittee Chair Bill Huizenga. The press release states that the working group will examine ways to "rein in the SEC's regulatory overreach; reinforce the materiality standard as a pillar of our disclosure regime; and hold to account market participants who misuse the proxy process or their outsized influence to impose ideological preferences in ways that circumvent democratic lawmaking."

McHenry stated that "[t]his group will develop a comprehensive approach to ESG that protects the financial interests of everyday investors and ensures our capital markets remain the envy of the world. Financial Services Committee Republicans as a whole will continue our work to expand capital formation, hold Biden's rogue regulators accountable, and support American job creators." Huizenga added that "[t]he SEC's climate disclosure rule is a prime example of this overreach that would have a wide-ranging impact on hard working Americans across all walks of life. I look forward to leading our committee's ESG working group, which will focus on promoting strong, vibrant capital markets, while defending the interests of all retail investors."

Taking the Temperature: The creation of the working group is yet another example, if one were needed, of the partisan divide in the U.S. on the subject of ESG. This announcement follows the establishment of the Congressional Sustainable Investment Caucus on January 25, a Democrat-led initiative that aims to "bring together Members of Congress with experts to better understand sustainable investing and inform policy making that provides investor protections and transparency of information to market participants." Two aspects of Representative McHenry's announcement bear mention. First, the press release seems to claim that the Working Group's approach is in line with Supreme Court precedent, observing that "last year, the Supreme Court ruled in *West Virginia vs EPA* that government bureaucracies cannot arbitrarily expand their own regulatory reach." While the Supreme Court, invoking the Major Questions Doctrine developed in its separation of power jurisprudence, held that an Environmental Protection Agency rule exceeded the EPA's authority under the Clean Air Act, the

decision rests squarely on the rule in question relative to the EPA's authority under the statute at issue. The Court found that the EPA effected a "fundamental revision of the statute," going from "ensuring the efficient pollution performance of each individual regulated source," whether it be coal, gas or another power source, to "demand[ing] much greater reductions in emissions based on a very different kind of policy judgment: that it would be 'best' if coal made up a much smaller share of the national electricity generation." Although the decision plainly is potentially relevant in cases challenging agency rulemaking, claiming the mantle of *West Virginia* without regard to the arguably unique facts of that case says little about the likelihood of the SEC's climate disclosure rule – the apparent main focus of the Working Group's dissatisfaction – surviving legal challenges. Which raises the second point, namely the Working Group's goal of "rein[ing] in the SEC's regulatory overreach." In its recent 2023 examination priorities letter, the SEC Division of Examinations made clear that ESG-related advisory services and funds will remain an area of significant focus. And, the SEC's final climate-related disclosure rule is expected to be issued in April 2023. In our view, however, attacks on the SEC rule or its examination priorities miss the crux of the issue. As we have commented, whether or not the SEC climate rule survives as proposed, or in modified form, or even if it is invalidated via court challenges (an outcome we think is unlikely given the SEC's investor protection mandate), companies need to consider and report on material risks, developments and opportunities, whether arising from climate issues, social impact movements, or other forces. Likewise, asset managers need to consider those same issues when making investment decisions as well as reporting on the sustainability characteristics of their investment portfolios – issues that have put them at the forefront of calling for greater issuer disclosure on ESG-related matters.

Aviva Outlines Stewardship Priorities for 2023

February 24, 2023

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In its **annual letter** to company board chairs, Aviva Chief Executive Mark Versey set out stewardship priorities for the coming year. The global asset manager, which has £232 billion ($279 billion) under management, states that it is "committed to help create a more sustainable, prosperous and inclusive future for our clients and wider society, while supporting our own ambition to become a net-zero company by 2040." Aviva's three key priorities "that will shape [its] stewardship activities as shareholders and bondholders in 2023" are: (i) tackling the cost-of-living crisis; (ii) transitioning to a low-carbon economy; and (iii) reversing nature loss.

Aviva expects all companies to prepare and publish "robust and financially viable climate transition plans that will support the decarbonisation of economies in a socially just and inclusive manner." The asset manager explains that they are "strong supporters" of the **UK's Transition Plan Taskforce (TPT) Disclosure Framework** and expect its recommendations to be integrated into the International Sustainability Standards Board guidance. Aviva will "encourage" companies to "pay particular attention" to several components of the TPT Disclosure Framework, including: describing the key impacts of the transition plan; estimating the impact of the plan on the financial position of the company; ensuring the transition plan is fully costed; integrating climate targets and metrics into variable incentive arrangements for executives and senior management; developing strategies to engage with customers, suppliers and partners to "collectively drive the decarbonisation of the entire value chain;" establishing Scope 3 emission reduction targets and report on the success of any initiatives; and engaging with governments, regulators and civil society to create an effective transition pathway.

Aviva references the **Global Biodiversity Outlook** and offers its expectation that companies "demonstrate how they are aligning their internal policies and practices with a nature-positive ambition and quantify[ing] the financial risks and opportunities associated with their dependencies and impact on nature." Furthermore, Aviva requests that companies begin reporting "within a reasonable timeframe" against the Taskforce on Nature-related Financial Disclosures framework, which is due to be finalized later this year. In advance of the completion of this framework, Aviva expects companies to carry out a business model assessment process.

Taking the Temperature: Aviva's stewardship priorities are another example of investors taking a more active role in seeking to influence the management and direction of companies in which they are shareholders. As would be expected from a large institutional asset manager, Aviva's approach is less aggressive than that taken by NGOs that have submitted resolutions requesting that financial institutions disclose their climate transition plans or have commenced litigation against companies and their boards for allegedly mishandling climate transition as reflected in published climate

transition plans. As a result of these suits, some companies may be reluctant to prepare climate transition plans, but based on a recent report published by CDP, there seems to be a clear, albeit slow-moving, direction of travel of companies disclosing some form of climate transition plan. Another noteworthy aspect of Aviva's letter is its focus on biodiversity and the related recognition that impacts on nature can have material effects on companies, concerns raised by BlackRock and other asset managers amid overall increasing attention being paid to the issue of nature-related climate impacts.

French Financial Regulator Calls for Review of SFDR Minimum Standards

February 24, 2023

By Duncan Grieve
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On February 13, the **Autorité des marchés financiers (AMF)**, the French financial regulator, **proposed** the introduction of legislation to establish "minimum environmental requirements" that must be met in order for financial products to be classified as Article 8 or Article 9 under the Sustainable Finance Disclosure Regulation (SFDR). The AMF explains that since the SFDR "does not impose minimum requirements and does not define the concept of sustainable investment . . . the current Article 8 and Article 9 classification does not aim to assess the nature or extent of the manager's commitment to sustainability."

As defined in the SFDR, Article 8 funds are those that promote Environmental or Social characteristics but do not have them as the overarching objective. Article 9 funds are those that have specific sustainable goals as their objective.

The AMF proposes that, "in order to avoid . . . ambiguity and to better meet the expectations of savers," the European Commission introduce minimum criteria concerning environmental impacts for products categorized under Articles 8 or 9. It suggests the following recommendations:

- Minimum environmental criteria should be established for the classification of products as Article 9 or Article 8. Compliance with these criteria would be subject to national supervision. The criteria for Article 9 should continue to be more stringent than those for Article 8.
- A minimum proportion of portfolio assets for Article 9 funds should consist of investments aligned with the Taxonomy. This percentage could increase over time as the European economy advances towards sustainability.
- Financial market participants that manage Article 8 and 9 funds should adopt a binding ESG approach in their investment decision-making process. The EU framework for minimum criteria should identify a set of acceptable ESG approaches that can be implemented by financial players.
- Article 9 funds should exclude investments in fossil fuel activities that are not aligned with the European Taxonomy. Investment in such activities would be possible for Article 8 products provided that they meet strict conditions that ensure that these activities are engaged in an orderly transition.

The SFDR recently received **criticism** from some European asset managers for its lack of clarity and precision. This **uncertainty** has led to a number of asset managers announcing that they are downgrading ESG funds from Article 9 to the less restrictive Article 8. In the fourth quarter of 2022, asset managers downgraded funds totaling 175 billion euros ($187 billion) of

assets from Article 9 to Article 8. In this same vein, in a response to a call for evidence on greenwashing by the European Securities and Markets Authority (ESMA), the Securities and Markets Stakeholder Group (SMSG) **recommended** further clarification of what qualifies for Article 8 and Article 9 fund classification under the SFDR.

Taking the Temperature: The perceived lack of precision on what constitutes a suitable Article 9 investment – *i.e.*, those that have specific sustainable goals as their objective – remains a major concern for asset managers. Funds are, understandably, hesitant to make sustainability-related claims or agree to strict criteria, such as the Article 9 classification, without clarity as to what constitutes a sustainable investment due to a risk of greenwashing challenges. This has not stopped all asset managers from establishing Article 9 funds. For example, Goldman Sachs recently announced that it had closed over $1.6 billion in funding for its Article 9 Horizon Environment & Climate Solutions I fund.