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Croatia, Hungary and Portugal Referred to the Court of Justice of the European Union by the European Commission

March 3, 2023

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On February 15, 2023, the European Commission referred Croatia, Hungary, and Portugal to the Court of Justice of the European Union for failing to transpose the EU's Renewable Energy Directive (Directive) into national legislation. In a **press release**, the EC stated that it was "hereby taking legal steps to ensure the development of renewable energy across the EU and to reduce greenhouse gas emissions, energy dependency and high prices."

The **Directive** was enacted on December 11, 2018 to further the EU's goal of promoting renewable energy. Among other things, the Directive created a common "legal framework for the development of renewable energy in electricity, heating and cooling, and transport," and "an EU-level binding target for 2030 of at least 32% renewable energy" in the EU's gross final consumption of energy. EU Member States were required to transpose the Directive by June 30, 2021, and immediately communicate such text to the EC. Despite first receiving a **reasoned opinion** from the EC in May 2022 urging them to comply with the transposition requirements, Croatia, Hungary, and Portugal failed to notify the EC of having done so.

Under the Treaty on the Functioning of the EU, Member States that do not comply with a reasoned opinion within the designated period of time are subject to **infringement procedures** and financial sanctions in the Court of Justice. **EC guidance** explains that "the sanction imposed by the Court may be composed of a lump sum payment, as a consequence of the continuation of the infringement until the delivery of its judgment or full compliance, if reached earlier, and a daily penalty payment, to prompt the Member State concerned to bring the infringement to an end as soon as possible after the delivery of the judgment." The Court of Justice has discretion to determine the amount of any sanctions imposed based on "three fundamental criteria: the seriousness of the infringement, its duration, [and] the need to ensure that the financial sanction itself is a deterrent to further infringements." The purpose of the sanctions regime "is to incentivise Member States to transpose directives" adopted by the EU within the proscribed deadlines "to ensure that [EU] legislation is genuinely effective."

Taking The Temperature: As we have previously reported, regulators in the U.S. and elsewhere have been commencing enforcement actions into greenwashing and other climate-related issues at an increasing pace over the past twelve months. Likewise, there has been significant rule-making activity regarding climate disclosure and

governance. At the same time, governments and government-funded multilateral development banks have been taking concrete steps to help finance green transition efforts. The EU's referral of Croatia, Hungary, and Poland to the Court of Justice continues this trend—which shows no signs of abating—of substantial overall government and regulatory activity arising from climate issues, albeit in a different context.

Review of Investor Voting on Environmentally Focused Shareholder Proposals in 2022

March 3, 2023

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On February 14, 2023, Georgeson LLC, the shareholder proxy solicitation firm, **published** an analysis of investor voting decisions in 2022 on certain types of shareholder proposals. In preparing its report, it looked at public filings by companies in the Russell 3000 Index. In total, Georgeson observed a total of 941 shareholder proposal submissions, a majority of which concerned ESG issues: 60 related to environmental matters, 231 involved social issues and 271 related to governance.

Georgeson reported that in 2022, 15 out of 60 environmentally focused shareholder proposals received majority support. This passage rate is marginally lower when compared to 2021, which Georgeson attributes to "heightened ambitions of some proponents this year, which is indicative of the amount of proposals discussing scope 3 emissions," and not a general decrease in support from investors of environmental-related proposals. The report explains that proposals advocating greenhouse gas emission reductions were the most common subject among environmental proposals that went to a vote (22 out of 60) and also represented a majority of the proposals that passed. Georgeson also observed that the fact that a significant number of greenhouse gas-related proposals did not go to a vote indicated that "issuers were more willing to negotiate with proponents on these proposals." The topic of companies' stewardship of resources including water usage, deforestation and plastics was covered in 10 of the proposals that went to vote (out of 60 originally submitted), of which two received majority approval.

Diversity equity and inclusion (DEI) was another "major theme" for shareholder proposals in 2022, with Georgeson reporting 44 DEI-related proposals that went to a vote. Georgeson commented on "the variety within DEI-related shareholder proposals," observing that in 2022, "shareholder proposals seeking DEI-related data requests included disclosure of recruitment, retention, and promotion information specifically addressing diverse employee populations, or reporting on steps by the company to implement their stated diversity and inclusion initiatives. In addition, in our research we looked at the civil rights audit and racial equity audit proposals, which gained momentum in 2022."

Taking the Temperature: Georgeson states that "[u]nlike prior proxy seasons, the 2022 proxy season can be characterized by increased scrutiny towards ESG matters." In our view, this development is based on a number of factors.

First, the SEC is proposing amendments to Exchange Act Rule 14a-8, and its Division of Corporation Finance issued Staff Legal Bulletin 14L (SBL 14L) in 2021, which taken together will make it easier for shareholders to require companies to include their

proposals in company proxy statements. SLB 14L is particularly significant. Currently, Rule 14a-8 allows a company to exclude a stockholder proposal that "deals with a matter relating to the company's ordinary business operations." Previously under this exception, companies could exclude proposals concerning social policy issues if the proposal was not material to the company's business. SLB 14L removed any requirement that there be a causal nexus between the social policy issue and the company's business. Now, the SEC will "consider whether the proposal raises issues with a broad societal impact, such that they transcend the ordinary business of the company."

Second, we have observed increasing shareholder proposal activity in relation to climate change, including on the part of public pension funds and NGOs.

Third, some of the largest institutional fund managers have been rolling out programs to provide their clients with greater say in how their shares are voted. If such investor-led voting schemes become widely adopted, given the high level of investors indicating policy preferences, it could have a substantial impact on the voting and governance landscape for public companies, including in areas as widely debated and significant as climate change.

EBA Seeks Input from Credit Institutions on Green Loans and Mortgages

March 3, 2023

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On February 13, 2023, as part of the European Commission's Strategy for financing transition to a sustainable economy, the European Banking Authority (EBA) launched an **industry survey** seeking input on green loans and mortgages and market practice relating to such loans. Credit institutions that intend to participate in the survey must contact their national competent authority to receive the survey templates as well as information on the process.

Participating credit institutions should reply to the survey no later than April 7, 2023.

Background

In November 2022, the EBA received a **Call for Advice** from the European Commission (EC) on the definition and possible supporting tools for green loans and mortgages for retail and small medium enterprise (SME) borrowers. The Call for Advice focused on four major areas:

- An overview on existing market practices: The EBA was invited to provide an overview of the green loans market and related market practices. This would include identifying the areas in which retail borrowers and SMEs are most active and would benefit from access to sustainable finance and also cover the standards and classifications in use for green loans in the market, public schemes in place to encourage green loans and mortgages in the European Union (EU), as well as an overview of gaps and regulatory barriers to the development of a green loan market.
- Green loan definitions based on the EU Taxonomy: The EBA was asked to propose specific features for a voluntary EU definition of green loans based on the EU Taxonomy Regulation (EU Taxonomy) and its disclosure requirements. This would include detail around key features and processes for the purposes of originating such loans, as well as assessing alignment with the EU Taxonomy criteria and sustainability assessment of collateral of green mortgages and loans. The EBA was also asked to consider the merits of such a definition, taking into account benefits, cost impacts, and any risks associated with the use of such definition.
- Measures to encourage and facilitate the uptake of green loans while ensuring the protection of retail borrowers: The EBA was requested to identify and assess potential legislative and non-legislative measures to encourage and facilitate the uptake of green loans by retail

borrowers based on the Taxonomy and stimulate the origination of such assets by credit institutions. The EC noted that the mitigation of any potential risks to consumers and SMEs are important considerations in this context.

- Green loan origination process: The EBA was requested to assess the merits of further specifying loan origination process requirements for credit institutions, with the aim to facilitate the development of the green loans market and their origination while also safeguarding credibility and consumer protection in the green retail loan market.

The EBA was requested to deliver advice by December 29, 2023, covering the most important types of green loans offered by credit institutions in the EU and focus on loans provided to retail borrowers, including green mortgages and other loans with environmentally sustainable features.

The request from the EC complements ongoing work on the EU sustainable finance framework including the Sustainable Finance Disclosure Regulation, the EU Taxonomy, and European Green Bonds Standard proposal.

Taking the Temperature: We have previously written on the inconsistent regulations across jurisdictions on climate-change disclosure. There is currently no consistently used EU-wide regulatory definition of what constitutes "green loans" and differences arise within members states. Industry definitions have been created by the Loan Market Association, the Loan Syndications and Trading Association, and the Asia Pacific Loan Market Association; however these are voluntary standards and are jurisdiction-agnostic. The survey is an important step towards creating a harmonized definition with a standardized approach, as well as alignment with existing regulation (such as the EU Taxonomy). The focus on consumer protection and SMEs in this context is an important consideration to create a just transition to a sustainable future in line with the overarching goals of the EU sustainable finance framework.

California Bill on Climate-Related Disclosure

March 3, 2023

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California Senate Bill 253, the **Climate Corporate Data Accountability Act**, if passed, will require all companies that do business in California and report over $1 billion in annual revenue to report on the full range of their emissions. Additionally, the disclosure would be subject to third-party review. The bill, which if enacted would become part of California's Health and Safety Code, was introduced on January 30, 2023 and is based on legislation that failed to advance in the previous session. The bill would require the California State Air Resources Board to adopt regulations, on or before January 1, 2025, requiring companies to publicly disclose their Scope 1, Scope 2, and Scope 3 emissions to an emissions registry. The reporting requirement would commence in 2026. This bill forms part of a broader climate accountability package that was introduced in the California Senate comprising three bills: the Climate Corporate Data Accountability Act (SB 253), the Climate-Related Financial Risk Act (SB 261), and the Fossil Fuel Divestment Act (SB 252).

This development is of particular interest given that the SEC is **expected** to issue its final climate-related disclosure rule in April 2023. The California bill differs in certain respects from the proposed SEC rule. Among other things, the California bill would apply to all "partnerships, corporations, limited liability companies, and other business entities" with over $1 billion in annual revenue, not just publicly traded companies. The California bill would require third-party audits of all emissions data, including for Scope 3 emissions, whereas the SEC rule is expected to only require third-party audits for Scope 1 and 2 emissions data. And while the SEC proposal is national in scope, the California bill has geographic limitations, applying only to entities "that do business in California."

There has been speculation that the SEC may eliminate or otherwise reduce the disclosure requirements regarding **Scope 3 emissions**. In its currently proposed from, the SEC rule would require issuers to disclose Scope 3 greenhouse gas emissions metrics only if deemed material, or if the registrant has set a greenhouse gas emissions reduction target or goal that includes its Scope 3 emissions. Those disclosures, if made, would not be subject to third-party attestation. The California bill proposes the same treatment for Scope 1, 2 and 3 emissions, including mandatory disclosure and attestation.

Taking The Temperature: The not-quite-overlapping California and SEC climate-disclosure proposals highlight the challenges companies face due to the lack of consensus on appropriate sustainability reporting. Reporting on Scope 3 emissions is particularly difficult because, among other things, by definition the relevant information is in the possession of entities in the company's value chain, not with the issuer itself, raising questions about the reliability and accessibility of that information as well as the quality of the data on which it is based. Requiring third-party attestation of Scope 3

emissions reporting, as California proposes, only heightens the risk and uncertainty around this disclosure item. On the other hand, California is not an outlier on Scope 3: the International Sustainability Standards Board, for instance, recommends that companies disclose information on Scopes 1, 2 and 3 greenhouse gas emissions. But more fundamentally, the existence of divergent disclosure regimes governing the same company is not tenable over the long term. Globally and nationally, regulators and regulated entities are seeking greater consensus on climate reporting requirements. We believe that is the direction of travel, but companies will need to wade through a thicket of guidance that at times is inconsistent before there is something resembling agreement globally on appropriate climate disclosure.