CADWALADER

June 6, 2023

June 6, 2023

Table of Contents:

Airline Sued Over Claims That it is “First Carbon-Neutral Airline”

June 6, 2023

By Sara Bussiere
Special Counsel | Global Litigation

On May 30, 2023, a **consumer class action lawsuit** was filed in the United States District Court for the Northern District of California asserting that the airline falsely claimed that it is the world’s “first carbon-neutral airline.” Plaintiff asserts three causes of action against Delta Air Lines: (i) violation of the Consumers Legal Remedies Act, § 1750; (ii) false advertising, Business and Professions Code § 17500; and (iii) unlawful, unfair, and fraudulent trade practices in violation of Business and Professions Code § 17200. Plaintiff claims that Delta relied on carbon credits to offset its reported emissions, but the benefits from those carbon credits are largely exaggerated and therefore, Delta’s reported emissions data is false and misleading.

Specifically, the complaint alleges that the voluntary carbon offset market “cannot make a company ‘carbon neutral’” because “the primary offset vendors offer offsets replete with” false data, including:

- “inaccurate accounting;”
- “non-additional effects on worldwide carbon levels due to the vendors crediting offsets for projects that would have occurred with or without market investment;”
- “non-immediate speculative emissions reductions that will at best occur over decades, despite crediting purchase with the sum of those projected offsets;” and
- “impermanent projects subject to disease, natural disasters, and human intervention.”

The complaint further alleges that because Delta’s carbon-neutrality claims are false and misleading, “consumers would not have purchased tickets on Defendant’s flights, or paid substantially less for them, had they known the claim of carbon neutrality was false.” Plaintiff claims that she paid a premium for Delta flights believing she was “engaged in more ecologically conscious air travel” and participating “in a global transition away from carbon emissions.” A copy of the 41-page complaint is available [here].

Taking the Temperature: This lawsuit represents one of the first private actions in the United States based on greenwashing claims. Though the case is in its very early stages, we offer some preliminary observations:

First, whether plaintiff is able to obtain class certification will serve as a potential indicator for both the strength of her claims and whether similar claims are likely to follow. Though Plaintiff asserts her claims on behalf of “[a]ll natural persons who, between March 6, 2020 and the present, purchased a Delta Airlines flight while located in California,” part of her theory is that, as someone in her late 20s, climate anxiety is

having a significant particular impact on Plaintiff and her generation. That novel theory aside, Plaintiff is likely to struggle with several elements of the asserted claims, including identifying cognizable damages. However, if Plaintiff is able to obtain class certification, then whether or not she ultimately is successful on the merits, such a result in and of itself could encourage additional consumer climate-focused litigation with respect to other industries and based on these or different theories.

Second, Plaintiff asserts a number of targeted attacks on the carbon offset market, an area that has triggered significant ongoing debate, including regarding the quality of the offsets vis-à-vis climate change mitigation as well as the potential benefits of, or need for, regulation of carbon offset markets. As we have previously written, Democratic senators have weighed in by asking the Commodity Futures Trading Commission (CFTC) for improved regulation of the market for carbon offsets in response to the CFTC's June 2022 request for information on climate-related financial risk.

ClientEarth Litigation in U.S. Over Deforestation in Brazil

June 6, 2023

By Jayshree Balakrishnan
Associate | Global Litigation

Environmental group ClientEarth has **filed a complaint** against Cargill, one of the world's largest soy and grain traders, over alleged deforestation and related human rights issues in Brazil. The **complaint**, which is not yet public, was filed with the Organization for Economic Cooperation and Development, pursuant to the Guidelines for Multinational Enterprises (OECD Guidelines). Under the OECD Guidelines, "companies are expected to conduct risk-based due diligence to identify, prevent and mitigate the actual and potential adverse environmental and human rights impacts of their operations." The **OECD Guidelines** apply to all companies operating in countries that participate in the OECD, such as the U.S. and Brazil.

ClientEarth alleges five breaches of OECD Guidelines by Cargill, primarily relating to its alleged lack of due diligence into environmental-related issues arising from its soy exports and production.

ClientEarth requests that Cargill fully disclose its current due diligence policies and procedures, and adopt and implement additional due diligence policies and procedures in line with global standards, with respect to its soy operations in Brazil. **Cargill's website** includes a sustainable soy policy and action plan, as well as a statement of commitment to "transforming our agricultural supply chains to be free of deforestation by 2030 ... It is founded on our belief that farming and forests can and must coexist."

Taking The Temperature: We have written extensively on the growing numbers of ESG- and climate-related litigation in 2023. Indeed, we have previously discussed ClientEarth's litigation in France against Danone over single-use plastics. This complaint against Cargill is yet another example of NGOs, individual civil plaintiffs, and enforcement authorities turning to legal process to address alleged greenwashing, including involving claims about adherence to articulated sustainability goals and commitments. Companies operating supply chains with deforestation and land use conversion risks should be proactive. Following the EU's new deforestation law and lawmakers' focus on curtailing deforestation in Brazil, companies should take care to ensure their global supply chains comply with local and global regulations, as well as any public statements regarding sustainability they have made.

ECB Reports Progress, Identifies Gaps in Banks' Climate-Related Disclosures

June 6, 2023

By Sukhvir Basran
Partner | Financial Services

In April 2023, the European Central Bank (ECB) published its **2022 assessment** of climate-related and environmental risk disclosures of EU-based banks, finding that while most "significant institutions" "now disclose at least basic information" in most climate-related categories, an improvement relative to the ECB's 2021 assessment, the quality of information remains "low and is unlikely to provide market participants with insights on which they can act." The report is the third such assessment carried out by the ECB as part of its wider objective to ensure that the European banking sector discloses climate and environmental risk effectively and comprehensively. The ECB's 2022 assessment examined 103 significant banks, all under direct supervision of the ECB itself, as well as 28 "less significant institutions." The ECB also examined the disclosures of 12 banks **from its list** of global systematically-important banks based outside the EU in order to provide an international benchmark.

The ECB observed considerable progress against previous years: the percentage of significant institutions that disclosed material exposure to climate and environmental risks was 86%, up from 36% a year ago. Approximately 85% of banks examined reported on their board of directors' and senior management's oversight of climate risks, up from about 70% in the previous review. More than 90% of institutions provided basic descriptions of their identification and management of environmental and climate risks. However, "banks still need to close remaining gaps to disclose all relevant [climate] risk information as only 34% of the banks disclose information on all categories," and the information disclosed remains "qualitative and often generic." Even where "metrics and targets are disclosed, banks often provide limited information on portfolio coverage and definitions and methodologies used to produce the respective information." With respect to governance disclosure in particular, the ECB identified as an area for improvement the need to provide "more detailed disclosures providing more precise information regarding the interface between the respective committees, the flow of information among the three lines of [defense], the bottom-up and top-down provision of information, the frequency of reporting and the transversal nature of climate-related risks as embedded in the risk management spectrum of the institutions."

Scope 3 financed emissions were an area of shift. Traditionally, Scopes 1 and 2 emissions have been mandatory to report, whereas Scope 3 has been voluntary, as they are the hardest to monitor. As Deloitte has **observed**, Scope 3 emissions are nearly always the major factor in corporate climate impact, often accounting for 70% or more of a business' carbon footprint. With the advance of both technology and regulatory oversight, companies are increasingly able to report all three types of emissions with greater accuracy. The most recent ECB report indicates that 50% of banks are now reporting Scope 3 financed emissions, however "in 85% of cases these are not (broadly) adequate. Overall, a mere 5% of banks made adequate or somewhat adequate disclosure on" all Scope 3 criteria.

The ECB also reported that banks, on the whole, are unprepared to comply with the European Banking Authority's (EBA) imminent **Implementing Technical Standards (ITS)** on Basel III Pillar 3 ESG risks. Pillar 3 requires a variety of ESG-related disclosures, including qualitative and quantitative information on transition and physical risks, exposure to at-risk sectors and green lending. In line with the final draft ITS, large institutions that have issued securities that are admitted to trading on a regulated market of any Member State will be required to make their first disclosures in June 2023.

Taking the Temperature: We have previously reported on the Basel III Pillar 3 requirements. Bank regulators globally are, like the ECB, demanding increasing ESG-related risk assessment and/or disclosure from financial institutions, with regulators in Canada, Switzerland, the U.S. and the UK, among others, weighing in with guidance. We also have reported on efforts by financial institutions to develop and disclose GhG emissions financing targets and ESG-related governance procedures.

With respect to its most recent assessment, the ECB is already taking action in relation to poor performers identified by its report. Six of the 15% of banks whose disclosures were considered insufficient overall were determined to be unsatisfactory in all disclosure categories. After publication, the ECB sent individual feedback letters to banks informing them of the outcome of the ECB's analysis of the shortcomings. The ECB observed that it had also sent requests to several banks to provide plans for how they will address their highlighted shortcomings in order to meet the EBA reporting requirements triggered by ITS in the near future.

The ECB has warned that non-compliance with these standards, having now come into effect for institutions listed in the EU, would constitute a violation of EU law. Frank Elderson, Vice-Chair of the ECB's Supervisory Board, told banks that "stricter disclosure rules are taking effect this year. If necessary, we will take the appropriate supervisory actions to ensure that banks comply." In anticipation of incoming obligation, banks and other financial market participants are already spending significant time and resources on compliance with new regulatory requirements. Financial institutions operating in the EU will want to ensure that they are closely monitoring and expanding their climate-related disclosure practices to keep step with changing expectations from the ECB and other national regulators.

European Parliament Adopts Corporate Sustainability Due Diligence Directive Amendments

June 6, 2023

By Duncan Grieve
Special Counsel | White Collar Defense and Investigations

On June 1, 2023, the European Parliament **adopted amendments** to the **corporate sustainability due diligence regulation and amending directive**. Under the amendments, large companies operating in the EU would be required to conduct due diligence to identify, prevent, mitigate or end negative impacts on human rights and the environment, including in particular pollution, biodiversity loss and environmental degradation, as well as labor exploitation, slavery and child labor. Covered entities would be required to produce climate transition plans to align their business models and corporate strategies with the Paris Agreement's goal of limiting global warming to 1.5°C above pre-industrial levels. The amendments were adopted with 366 votes in favor, 225 against, and 38 abstentions.

Last month, the Legal Affairs Committee of the European Parliament (known as Juri) approved these new **corporate due diligence rules** in line with the European Commission's proposed **Corporate Sustainability Due Diligence Directive** of 2022.

More entities—and individuals—covered

The proposed rules expand companies' due diligence obligations beyond their own activities to include their value-chain—including suppliers as well as any entities related to sale, distribution or transportation. Covered companies would have to mitigate any adverse impacts as a result of value chain relationships by changing company business models, providing support to small and medium-sized entities (SMEs) in the value chain, or seeking contractual assurances from partners.

The amendments expand the categories of covered entities from those originally proposed by the EC to include EU-based companies with more than 250 employees and a net annual revenue worldwide of at least 40 million euros; parent companies with more than 500 employees and a net annual revenue worldwide of at least 150 million euros; or non-EU companies with $150 million net annual revenue if at least 40 million euros were generated in the EU.

The rules also impose requirements on directors to implement tailored transition plans aligning their companies with the Paris Agreement. Notably, the largest companies—those with more than 1,000 employees on average—"should have a relevant and effective policy in place to ensure that a part of the directors' variable remuneration is linked to the achievement of the targets of the company's transition plan for combating climate change."

Under the proposal, covered entities would be obligated to engage with key stakeholders, monitor the effectiveness of their due diligence programs and policies, and create a grievance mechanism for concerned stakeholders. How engagement, monitoring and reporting will work, as well as penalties for failure to comply with these requirements, remains unclear.

Financial sector exemptions

Whether and to what extent the financial sector would be subject to the directive has been a much-discussed issue. Financial institutions were originally excluded from the proposed directive, but the adopted amendments require institutional investors and asset managers specifically to comply with the directive, including conducting due diligence on their clients.

Enforcement framework and timetable

Under the amendments, companies that violate these requirements would be sanctioned in the form of "naming and shaming," removing the companies' goods from the market, or fine at least 5% of total revenue for EU companies. Failure to comply with the proposed rules could also make companies vulnerable to litigation. Non-EU companies could also be subject to a ban from public procurement in the EU.

The new obligations under the amendments, if adopted, would take effect in 3 or 4 years depending on the company's size.

Status of the directive

Now that the proposal has been adopted, negotiations with the EU Council and member states will begin. Member states previously reached a consensus on the directive in EU Council at the end of 2022, but certain issues, including the exclusion are for certain financial services entities, are likely to be heavily discussed. Parliament and the EU Council must agree on a position before further negotiations with the European Commission to finalize the directive.

Taking the Temperature: As the European Commission noted in its February 2022 statement announcing the proposed directive, a number of EU member states, including France, the Netherlands, and the UK, already have national ESG due diligence rules. The EU-wide directive is intended to harmonize enforcement and civil and criminal liability frameworks, as well as scale up efforts across the bloc.

Critics on both sides of the debate have weighed in as to whether the proposed directive hits the mark or is overkill that will have a deleterious economic impact. Environmental activists point to what they consider to be gaps in the new rules, including the exemption of some financial institutions and the proposed delays in the enforcement timeline. On the other side, member states and industry representatives have pushed back on the scale and ambition of the current EU environmental regulation drive, as well as the timeframe. Recently, French President Emmanuel Macron called for a pause in EU regulation-making to give member states time to implement existing regulations, noting that the EU is already at the forefront of environmental regulation. Critics of the proposed due diligence directive, in particular, say that the scale of the required oversight across the value chain is unwieldly at best, and at worst, impossible to achieve. Industry groups also cite the potential of the proposed directive to dampen investments and open the floodgates for litigation against companies.

On that last point, as we have previously discussed, a variety of litigation will almost certainly follow, once the final rules have been negotiated and put in place. The increased focus on creating incentives for director engagement is also notable—and an area of debate. As we observed here, the trend towards enforcement of environmental priorities through executive compensation is one that exists beyond the European Union.

Investor Coalitions Urge Consumer Goods Companies to Take Action to Reduce Plastics

June 6, 2023

By Jason Halper
Partner and Co-Chair | Global Litigation

In a **statement** released on May 3, 2023, the Dutch Association of Investors for Sustainable Development (VBDO) called for companies in the fast-moving consumer goods (FMCGs) and grocery retail sectors to reduce their dependence on single-use plastic packaging. The investor group is calling on companies and other market participants to "bring production and consumption of plastics within the limits of planetary boundaries and alignment with the Paris Agreement and the Kunming-Montreal Global Biodiversity Framework," warning that "clean-up is futile" if production continues at current rates. VBDO is an independent group of investors comprising more than 185 organizations with more than $10 trillion in assets under management that describes itself as a driver, motivator and knowledge leader for responsible investment.

VBDO notes that plastics are costly to society, imposing $350 billion in costs related to greenhouse gas emissions and ocean pollution. The investors also pointed out that companies involved in producing single-use plastics are increasingly exposed to financial risks as a result of both efforts by policymakers to address plastics-related environmental crises and mounting societal pressure for these companies to be held accountable. Those risks include regulatory challenges, responsibility costs, reputational issues, plastic-related regulation and increased raw materials costs, resulting in higher costs and lost business opportunities for companies that fail to address those risks.

The investor group also says that actions taken by companies in this sector—many of which are signatories to the **Ellen MacArthur Foundation-United Nations Global Commitment** — have so far failed to have a significant impact on the scale and at the rate required, in particular to meet the Global Commitment 2025 goal for all packaging to be reusable, recyclable and compostable.

The investors called on the FMCGs and grocery retail companies to make "real and scalable change"—"setting more ambitious targets and taking stronger actions" to "drastically reduce production and consumption of single-use plastic packaging and phase out hazardous chemicals[.]" The statement also called on companies to lobby for and not against "the policy framework needed to support these actions."

To accomplish these goals, the investors presented three expectations of the companies that intensively use plastic packaging:

1. Support ambitious plastics policies for effective outcomes, including by supporting a Global Plastics Treaty currently being negotiated, joining the Business Coalition for a

Plastics Treaty, advocating for legally binding measures that would reduce production and consumption of single-use plastics, boosting reuse of plastic products, and publicly supporting—and not lobbying against—the European Commission’s efforts to reform the Packaging and Packaging Waste Regulation (PPWR).

2. Commit to and achieve an absolute reduction of single-use plastic packaging by developing and implementing a clear plan of action that prioritizes eliminating single-use packaging altogether and scales up reusable packaging systems, including defined timelines and external verification.

3. Address toxicity in value chains by committing to identifying and eliminating the use of hazardous substances in products and packaging, and publicly reporting their progress.

Taking the Temperature: As we have reported previously, the environmental impact of plastics continues to be a focus for governments and regulators, investor coalitions, and environmental groups across the globe. Nor is this the first time that an investor group has been formed to engage with consumer good companies over the issue of plastic use. The environmental advocacy group As You Sow organized the formation of a coalition of institutional investors, the Plastic Solutions Investor Alliance, to engage with leading consumer goods companies on the threats posed by plastic pollution. As of the end of 2022, the coalition comprised more than 50 investors that had signed the Investor Declaration on Plastic Pollution aimed at compelling companies that use plastic packaging to take action, including: disclosing plastic packaging use; setting goals to reduce plastic packaging and develop recyclable, reusable or compostable packaging; taking “producer responsibility” for plastic packing use and taking a role in funding and facilitating recycling or composting of packaging; and supporting public policy measures on reducing plastic waste.

At least one environmental activist group has decided to litigate rather than simply encouraging companies to act in this area. As we reported in January, environmental nonprofit ClientEarth, along with other activist groups, brought suit against global food-products company Danone, alleging that the company has breached France’s Corporate Duty of Vigilance Law for failing to have an adequate plan to reduce its plastic footprint. Prior to filing the claim in a Paris court, ClientEarth served “legal warnings” on Danone and other French companies, including Auchan, Carrefour, Casino, Lactalis, McDonald’s France, Les Mousquetaires, Picard and Nestlé France. This indicates that other similar actions may follow, including possibly in other jurisdictions.