Cadwalader Climate

February 15, 2024

ESG Ratings

The European Council and Parliament **provisionally agreed upon a proposed regulation** on ESG rating activities to boost transparency and increase investor confidence in ESG ratings. ESG ratings providers would be regulated by the European Securities and Markets Authority (ESMA) and would have to be authorized and supervised by ESMA. Ratings providers established outside the EU would need to be either endorsed by an EU-authorized provider, recognized based on certain quantitative data, or subject to an equivalence decision. The proposed Regulation allows for the option to provide separate E, S and G ratings, but in such cases would need to detail the weightings of E, S and G factors. Once the new rules are formally adopted by both institutions, they would begin applying within 18 months. **We have discussed at length** the lack of consistency among ESG ratings providers and established industry norms relating to disclosure, measurement methodologies, transparency and quality of underlying data. That has led to a number of jurisdictions proposing regulations, with the EU being chief among them.

Continuing on the topic of ESG ratings, **in its latest ESG Commitment Level analysis**, Morningstar reported that eight of 97 global asset managers have met their highest ESG commitment level. Dubbed “Leaders,” this roughly 8% scored higher than the 24% classified as “Advanced,” 45% as “Basic” and 23% as “Low.” Still, the ratings agency reported that the majority of firms have shown improvement in their practices. Morningstar’s ESG Commitment Level provides investors with information related to an asset manager’s sustainable-investing philosophies, ESG integration processes, resources and active ownership activities.

Anti-ESG Sentiments

In last week’s edition, we discussed the SEC’s climate disclosure rule and how the delay in its implementation has not hindered developments elsewhere, including in California, where two corporate climate disclosure laws (Senate Bills 253 and 261) recently have been enacted. California is now being sued over these laws by, among others, the U.S. Chamber of Commerce (USCC), which argues that the state is unconstitutionally compelling speech. The American Farm Bureau Federation, four other groups and the USCC claim that the laws “unconstitutionally compel speech in violation of the First Amendment and seek to regulate an area that is outside California's jurisdiction and subject to exclusive federal control by virtue of the Clean Air Act and the federalism principles embodied in our federal Constitution.”

Greenwashing in the Ultra Low Emissions Zone

A recent action in the UK highlights the increased scrutiny of environmental claims in advertising materials by regulatory authorities. **The Mayor of London has been warned** that Transport for London’s (TfL) environmental claims relating to its Ultra Low Emissions Zone (ULEZ) may be misleading. The Advertising Standards Authority (ASA) received 503 complaints relating to six claims, which included, “The Central London ULEZ has shown you can reduce air pollution, we have seen almost a halving of levels of nitrogen dioxide," "The ULEZ has already made a significant difference by helping to reduce harmful nitrogen dioxide pollution by nearly half" and "Did you know that most air pollution related deaths actually occur in Outer London areas?" Other complaints related to claims connecting air pollution with deaths occurring in Outer London areas, and being linked to dementia. In its defense, TfL cited, among other things, research conducted by the UK Government and the World Health Organization (WHO) showing the impact on health that air pollution had, in addition to air quality modelling undertaken by Imperial College London. The ASA upheld complaints in relation to three of the six claims: in relation to levels of nitrogen dioxide, the ASA dismissed the evidence provided since, in its view, none of it backed up the claims made, and further that the advertising did not make it clear that the claims were based on "modelled estimates" and not on actual figures. The ASA directed TfL to ensure that the basis of all environmental claims was made clear in future ads. In response, the TfL expressed its disappointment at the ruling but, noting that the ASA did not dispute the science, stated that it would take care with its wording in future. In order to assist advertisers making environmental and sustainability-related claims to consumers, **the ASA published updated guidance**. This latest update from the regulator demonstrates the ASA's continued pursuit of what are, in its view, misleading unsubstantiated environmental claims. The ASA previously has taken action against misleading advertising campaigns in the **financial services** sector, **energy** sector and against **airlines**.