CLEARY GOTTLIEB

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Climate and the Financial Sector

This weekly newsletter highlights climate-related regulatory, litigation and enforcement developments relevant to the financial sector.

General

18 April 2023 [EU] – **EU Parliament adopts revision of EU Emissions Trading System and Carbon Border Adjustment Mechanism Regulation proposals at first reading**

The Parliament has formally adopted two elements of the Commission's 2021 "Fit for 55" regulatory package, concerning the future of ETS and CBAM. The vote follows the agreements reached with the EU Council on both texts in December 2022, with the Council expected to hold a similar conclusive vote in the course of the next weeks. This revision of the ETS will lower emission caps for the various sector covered, as well as (over-time) freely allocated emission allowances. It will also expand the system to real estate (in connection with the heating of buildings) and road transport, initially under a separate "ETS II" market. Imports of iron, steel, cement, aluminium, fertilisers, electricity and hydrogen into the EU will be subject under CBAM to a levy, corresponding to the price difference of carbon in the country of origin. [link]

18 April 2023 [EU] – **Activists groups challenge classification of natural gas as sustainable fuel**

ClientEarth, the WWF and other environmentalist NGOs have filed a case before the EU Court of Justice against the Commission's refusal to remove methane from the EU Taxonomy's Climate Delegated Acts (DAs). On the same day, Greenpeace filed a similar challenge targeting both methane and nuclear. If these proceedings were to succeed – leading to a review of the Climate DAs' relevant provisions –the "green asset ratio" of banks, investment firms and asset managers exposed to these sectors would be negatively affected. [link]

20 April 2023 [Global] – **Financial Stability Board reports on climate-related financial risk factors in compensation frameworks**

The FSB has issued a review of compensation practices around climate-related objectives, noting their increasing diffusion among global financial sector firms. It looks at how companies' climate goals are incorporated into their compensation frameworks overall, and identifies common challenges – such as data gaps, metrics reliability and misalignment of timeframes between compensation and assessment periods (on the one hand) and the – much more delayed – materialisation of climate-related risks (on the other). The report indirectly encourages firms to continue to revise and adapt their climate adaptation metrics, to ensure prudent risk management overall. [link]

Banking

18 April 2023 [UK] – **BoE climate lead delivers speech urging UK banks and insurers to consider impact of different climate scenarios**

Sarah Breeden (Executive Director for financial stability strategy and risk) said UK firms recognised a growing sensitivity of UK financial sector firms to climate, while at the same time reiterating that companies should continue to explore how different climate-change scenarios are relevant to their business strategy. She pointed to the tools developed by the BoE – encouraging vulnerability testing across all of four core dimensions: scenario analysis; firm risk management capabilities; disclosure; and green finance – and reminded firms of the homework set out in the BoE's latest "Dear CEO" letter and in direct supervisory feedback. Beyond just risk management, Breeden noted also climate-related opportunities, which the UK's first climate scenario exercise (CBES) showed were greatest with an early and well managed transition. [link]

21 April 2023 [EU] – **ECB issues 2022 report on banks' climate-related and environmental risks disclosures**

The European Central Bank has published the results of its third assessment of bank's environmental disclosures, based on the supervisory expectations of its 2020 "Guide on Climate-related and Environmental Risks". While the report recognises that the majority of banks now disclose basic information for most of the expectations set out under the Guide, it also notes that the quality of the disclosures remains low and is unlikely to provide market participants with insights on which they can act. Strategy, and metrics and targets are the aspects on which public disclosures are found to be most lacking. The release of the ECB's report takes place just as large listed EU banks prepare to issue their first Pillar 3 disclosures on ESG risks, due starting this year under Article 449a CRR. [link]

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