CLEARY GOTTLIEB

14 November 2022

Climate and the Financial Sector

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

EU Updates

General

9 November 2022: International Organization of Securities Commission (IOSCO) publishes draft recommendations for well-functioning voluntary carbon markets

Global securities regulators' body IOSCO issued a report relating to markets for voluntary carbon credits (VCCs). The report identifies three main concerns relating to VCC markets: (i) the quality of methodologies for issuing VCCs, including problems such as carbon leakage and lack of permanence of carbon reduction/removal projects, (ii) uncertainty as to the regulatory treatment of VCCs and lack of regulatory market oversight, and (iii) risks of greenwashing by companies that make use of VCCs. IOSCO invites feedback on the report by 10 February 2023 (here).

9 November 2022: IOSCO also consults on carbon compliance markets

On the same date, IOSCO launched a public consultation on carbon compliance markets (such as the EU's flagship Emissions Trading System), to support countries in setting up new carbon markets or improving their existing ones. The consultation considers both primary markets (*e.g.*, government-led initial allocation or auctioning of emission allowances) and secondary markets (*e.g.*, free spot or derivatives trading of allowances between market participants). In relation to primary markets, the consultation takes note of carbon leakage, oversupply of allowances and market stability mechanisms-related issues. For secondary markets, it focuses on market conduct, orderly trading, market integrity and transparency and oversight. The report also considers the benefits of international or globally-linked compliance markets, which could promote globally consistent carbon prices. IOSCO invites feedback on the report by 10 February 2023 (here).

COP27:

8 November 2022: World Benchmarking Alliance's new "Financial System Benchmark" highlights financial sector's fragmented and inadequate approach to tackling climate change

The World Benchmarking Alliance (WBA) – a global industry group aiming to shape the private sector's contribution to the UN Sustainable Development Goals – published a report assessing the progress made by 400 global financial institutions in supporting a just and sustainable transition. The report describes the financial sector's current approach to tackling climate change and protecting human rights as "*fragmented, siloed and insufficiently aligned to drive scale*". Commitments to net-zero remain low, with "*virtually no interim targets and tracking in place*". Financing to low-income countries, SMEs and other excluded groups is also labelled as insufficient (here and here).

8 November 2022: UN High-Level Expert Group issues report on financial sector net-zero greenwashing

The UN High-Level Expert Group on the Net-Zero Emissions Commitments of Non-State Entities (UNHLEG) published a report on net-zero commitments by businesses, financial institutions, cities and regions. The report notes that while net zero pledges have become a strong trend, some underestimate the task of having to implement them, or may not even intend to achieve the goals announced. The report provides several recommendations for companies including on setting of net zero targets, the use of voluntary carbon credits and the creation of transition plans. The report also includes a list of calls to action for regulators and standard setters (here).

9 November 2022: Future of Sustainable Data Alliance launches review of critical ESG data gaps for financial institutions

The Future of Sustainable Data Alliance (FoSDA) – a global alliance of institutions, companies and universities, aiming to identify and accelerate the reliable, actionable ESG data and related technology – has launched a review of corporate and sovereign ESG datasets, critical for improving sustainability disclosure and analysis. FoSDA also issued an update to its analysis of corporate ESG data and sustainability disclosures. Despite collaborative efforts to align corporate sustainability reporting frameworks, the report denounces holes and gaps as an enduring feature of social and environmental datasets. Key data points which the report identifies as "must-haves" from a climate impact perspective include GHG scope 1-2-3 emissions and temperature alignment (here and here).

9 November 2022: Net-Zero Banking Alliance publishes its first Progress Report

The Net-Zero Banking Alliance – a global industry group currently representing about 40% of global banking assets, committed to 2050 net-zero targets – published its first progress report. The report sets out intermediate 2030 decarbonisation targets for over 60 member banks, showing how members' initial decarbonisation efforts focus on highly emitting sectors such as power generation, oil & gas, and coal. The report also details the Alliance's efforts to support members in setting and implementing targets, including through the publication of guidance documents. The Net-Zero Banking Alliance calls for support from policymakers in creating a supportive regulatory environment that will facilitate an orderly and "whole-economy" transition to net zero, including, in particular, the need to meet institutions in committing to the Paris Agreement's target of 1.5°C (here).

10 November 2022: European Parliament adopts amended draft of the Corporate Sustainability Reporting Directive

The European Parliament has approved in plenary vote a draft of the Corporate Sustainability Reporting Directive (CSRD), which reflects the recent interinstitutional negotiations carried out with the EU Council. The CSRD will impose new, detailed ESG-related reporting requirements on an estimated 50,000 large and listed EU companies. Reporting requirements will look at both ESG risks and negative impacts (under the EU's "double materiality" approach to ESG). Sustainability reporting under the CSRD will be subject to independent auditing. The EU Council is expected to vote on the draft on 28 November. If the draft is approved, the new rules will begin applying to reports issued for FY 2024 (here). Access our analysis of the Commission's 2021 CSRD proposal here.

Banking

9 November 2022: EBA reaffirms commitment to increasing sustainability of the banking sector robust management of ESG-risk

The EBA has published a statement highlighting its work on increasing sustainability of the European banking sector through greater transparency, and dedicated risk management practices and supervision. In particular, the EBA discusses standards for

Pillar 3 disclosures of key ESG risks, its work to ensure robust management of ESG risks by institutions, recent supervisory efforts (including climate stress tests) and the discussions on the prudential treatment of exposures to ESG risks in the financial system (here).

Asset Management

7 November 2022: IOSCO issues call for action to counter greenwashing by asset managers, and ESG rating and data providers

IOSCO published a "Call for Action" addressed to voluntary standard setting bodies and financial industry associations, aiming to provide investors with internationally consistent and comparable sustainability-related information. Building on a November 2021 report, IOSCO sets out a number of "Good Sustainable Finance Practices". In particular, the report calls on asset managers to improve sustainability-related practices, policies, procedures and disclosure in their industry, and in ratings and data providers to improve the reliability, comparability, and interpretability of their ESG ratings and data products (here and here).

9 November 2022: Total assets under management of Net Zero Asset Managers Initiative grow to over USD 66 trillion; 86 additional asset managers disclose net-zero targets

The Net Zero Asset Managers (NZAM) initiative is a group of international asset managers committed to achieving the 2050 net zero invested assets goal. On 9 November, NZAM announced that the total number of its members had grown to 291, representing more than USD 66 trillion in global AuMs. It also noted that 169 of its members have so far set initial emissions reduction targets, all publicly available on the Alliance's website (here and here).

9 November 2022: Refinitiv Lipper issues Q3 2022 report showing sustained capital inflows for Article 9, in contrast with an outpour for Article 8 financial products

Refinitiv, (a financial data provider part of the London Stock Exchange group) issued its Q3 2022 report on the European ESG Fund Market. The report notes that both conventional and ESG-related *money market funds* witnessed net capital outflows over the quarter. Within long-term financial products, SFDR-dubbed Article 9 funds witnessed net capital inflows (of over EUR 32.8 bn), whereas Article 6 and Article 8 funds faced net outflows (of EUR 4.8bn and 173.1bn respectively). The report attributes this partly to growing regulatory and market pressure against greenwashing, and the absence of clear standards for SFDR categorisation, particularly with respect to Article 8 funds (here).

10 November 2022 : French AMF modifies its policy to facilitate

implementation of SFDR technical standards by asset managers

The SFDR's Regulatory Technical Standards (RTS), set to enter into force on 1 January 2023, will introduce detailed disclosure requirements in respect of Article 8 and Article 9 products. Under prior AMF policy, the introduction of these requirements would have required all funds to issue "investor letters" (typically used to flag significant modifications or deteriorations in a fund's position). The AMF's policy change scraps the need for French asset managers to issue letters at the start of the new year (here).

Amélie Champsaur
Partner, Paris
achampsaur@cgsh.com

Clara Cibrario Assereto
Associate, Rome
ccibrarioassereto@cgsh.com

Andreas Wildner
Trainee Solicitor, London
awildner@cgsh.com

Pierre Mathé
Associate, Paris
pmathe@cgsh.com