Akin

Speaking Sustainability

Sustainability/ESG Policy and Regulatory Update

March 2024

Akin's newsletter on environmental, social and corporate governance (ESG) policy and regulatory developments, provides a timely digest of ESG topics, news items and other relevant information regarding significant ESG policy headlines and debates concerning each ESG pillar. We also keep you up to date on activities in the state legislatures across the country. This newsletter is a companion to our existing weekly Climate Policy Update, which you can find at our Speaking Sustainability site.

Key ESG Topics

The SEC will vote on its long-awaited climate disclosure rule on Wednesday, March 6, 2024. It has been reported that the final rule will drop its Scope 3 disclosure requirements, a move Akin anticipated and discussed in these podcasts (Part 1 and Part 2) following the release of the proposal.

- Akin will be available to answer your questions after the release of the rule.

Institutional Shareholder Services Inc. (ISS) and Glass Lewis recently issued 2024 their proxy voting guidance.

- Akin's client alert can be found here and we are available to answer any questions you may have regarding such voting guidance as we head into the 2024 annual reporting and proxy season and its implications for ESG considerations.

The European Union (EU) announced new greenhouse gas emissions targets which will seek to reduce net emissions by ninety percent by 2040. The new targets are intended to support the EU's "Green Deal" goal to achieve climate neutrality by 2050.

- The new emissions goal would deepen emissions cuts by two percentage points compared to the current pathway and "entail a broader phase-out of fossil fuels, rapid electrification of road transport and heating sectors, a strengthened industrial policy with funding mechanisms and a plan to attract private capital."

- The announcement comes amid protests by farmers and industrial stakeholders in the bloc arguing the cost of the climate transition is too costly. This is causing some critics to label the new targets as "tone-deaf" and insensitive to the concerns highlighted by the protests.

- Lawmakers acknowledge the new targets will require significant international cooperation and innovative financial incentives to support these efforts and garner support from anxious stakeholders.

California's ESG-related corporate disclosure requirements are expanding. In October 2023, California Governor Gavin Newsom signed into law two climate bills (Senate Bill 253, the "Climate Corporate Data Accountability Act" and Senate Bill 261, the "Greenhouse Gases: Climate-Related Financial Risk" Act) and one mandating diversity disclosure within the venture capital industry (Senate Bill 54, the "Fair Investment Practices by Investment Advisors" Act). Both bills face legal challenges as a coalition of businesses filed a lawsuit on January 30 seeking to block implementation of the disclosure measures.

- California became the first state in the nation to require companies of certain revenues to disclose greenhouse gas (GHG) emissions from direct and indirect operations and supply chains, as well as report on climate-related financial risk and any measures adopted to mitigate those risks. Akin authored an **article** summarizing the two bills.

- **SB 253** requires corporations that operate in California and with total annual revenues greater than $1 billion to publicly disclose their annual scope 1 emissions (direct emissions from operations) and scope 2 emissions (indirect emissions from purchased energy) beginning in 2026, and scope 3 emissions (upstream and downstream emissions associated with products and supply chains) beginning 2027. Disclosure requirements are expected to align with the Greenhouse Gas Protocol.

- **SB 261** mandates companies with over $500 million in annual revenues and that operate in California to prepare a report, beginning in 2026 and every other year thereafter, on its climate-related financial risks consistent with the framework of the Task Force on Climate-Related Financial Disclosures (TCFD). The bill is intended to provide transparency into a company's climate-related economic impacts and associated risks, in addition to describing its implemented or planned mitigation measures.

- **SB 54** directs covered entities in the venture capital industry to report to the Civil Rights Department on the diversity of the founding members of businesses in which they invested during the prior year.

- As expected, SB 253 and SB 261 are currently being challenged in court by a business coalition led by the California Chamber of Commerce and the American Farm Bureau. The lawsuit argues the bills violate First Amendment rights by "forc[ing] thousands of companies to engage in controversial speech that they do not wish to make, untethered to any commercial purpose or transaction."

The 28th Conference of Parties (COP28) to the United Nations Framework Convention on Climate change (UNFCCC), commenced November 30 in Dubai, United Arab Emirates (UAE), and concluded December 12, 2023. Akin provided regular updates on the conference.

- A key objective of COP28 was to "accelerate an [energy] transition that puts our economies on the path toward a new low-carbon, high-growth, sustainable economic model in a way that is both transformational and just."

- Akin authored a COP28 "**preview piece**" that summarized the challenges, opportunities and anticipated outcomes of the conference. Themes include the first global stocktake (GST), Article 6 of the Paris Agreement, methane emissions and climate financing.

- COP28 opened with parties quickly adopting a framework for operationalization of a loss and damage fund intended to provide financial support to vulnerable countries coping with permanent (loss) or transitory (damage) impacts caused by climate change. The fund received more than $420 million in voluntary opening-day pledges.

Environmental

Clean Vehicle Tax Credit - Foreign Entity of Concern Rules Proposed (Akin)

The Department of the Treasury and Internal Revenue Service (IRS) proposed regulations intended to provide guidance regarding the excluded entity provisions with respect to the clean vehicle credit as amended by the Inflation Reduction Act of 2022 (IRA).

The U.S. Securities and Exchange Commission's Scrutiny of Greenwashing Risks Continues with Modifications to the '40 Act Names Rule (Akin)

The U.S. Securities Exchange Commission (SEC) issued a final rule amending the so-called "Names Rule" (found **here**) that is "designed to modernize and enhance" protections under Rule 35d-1 of the Investment Company Act of 1940. The final rule is part of the SEC's holistic efforts to regulate ESG matters, and is the SEC's latest attempt to curb greenwashing in U.S. capital markets.

How AI Can Help Clean Up the Biggest Climate Messes (*BNN Bloomberg*)

A new Japanese-led report on the use of artificial intelligence (AI) as a climate tool was presented at COP28 and particularly targets steep emissions cuts in hard-to-decarbonize sectors, such as steel and cement. The report cites machine learning models utilized at steel plants that improve efficiency, increase recycled feedstock and leverage historical data to minimize energy consumption.

U.S. Treasury Says Financiers' "Net Zero" Pledges Must Align With Temperature Limits (Reuters)

The Department of the Treasury unveiled its new, voluntary "**Principles for Net-Zero Financing & Investment**" during Climate Week 2023. The nine principles include guidance for banks and asset managers to align their net-zero financing commitments with limiting the global temperature increase to 1.5 degrees and are largely focused on scope 3 financed emissions.

A New Era for Corporate Disclosure of Nature-Related Risks (*Bloomberg*)

The Taskforce on Nature-related Financial Disclosures (TNFD) released its final recommendations for corporate disclosure. It is structured similarly to the four-pillar approach in the TCFD.

Social

U.S. Judge Will Not Block Biden Rule on Socially Conscious Investing (Reuters)

A federal judge in Texas dismissed a lawsuit filed by 25 attorneys general challenging the U.S. Department of Labor's (DOL) final ESG rule that allows fiduciaries to consider ESG factors when making retirement investing decisions. The judge concluded the rule does not violate the Administrative Procedure Act because it is not "arbitrary and capricious" and does not infringe on federal law that sets standards for retirement plans.

[Is Race a Major Factor Behind Opposition to Wind Farms?]() (*Inside Climate News*)

The Proceedings of the National Academies of Science **published** a paper examining local opposition to wind farms and the influence of white residents in halting a project compared to non-white residents—a study which Inside Climate News debates using its own research on challenges to wind farm development.

Investors Warn "Fluffy" ESG Metrics Are Being Gamed to Boost Bonuses (*Financial Times*)

Investors are raising concerns that ESG-related metrics are being taken advantage of by executives looking to increase bonus payments, particularly in employee engagement and diversity, equity & inclusion (DEI). Unlike financial metrics that are tied to earnings or share price performance, critics argue that ESG renumeration policies are nebulous, easy to manipulate and subjective.

SEC Could Be Moving Toward Regulation Of DEI In The Financial Industry (*Forbes*)

The SEC **released** its Diversity, Equity, Inclusion and Accessibility (DEIA) Strategic Plan for fiscal years 2023-2026. The Plan is primarily focused on internal policies and divided into three pillars—People, Culture and Mission—however, the plan includes two actions suggesting the agency will use its authority to promote implementation of DEI policies in the financial services industry.

Governance

SEC Director of Enforcement Announces a New Paradigm for Assessing Compliance Efforts (Akin)

The Director of the SEC's Enforcement Division gave a keynote address at the New York City Bar Association's 2023 Compliance Institute targeted at compliance officers in the private funds space. The Director emphasized "proactive compliance" will soon replace SEC's assessment of a firm's "culture of compliance," offering a three-factor rubric against which a CCO and a compliance program can be assessed: education, engagement and execution.

Companies Face Challenges Over ESG Reporting Requirements (*Board Agenda*)

As ESG disclosure begins to place more emphasis on the strategies companies implement to achieve their stated goals, mitigate risk and explore opportunities, this article suggests board members should begin formulating disclosure strategies and undertake materiality assessments to understand ownership of the company's respective data needs.

Recent ESG Rulemaking, Examination and Enforcement Activity (*Private Equity Law Report*)

This article outlines the SEC's bolstered approach to ESG, starting with the prioritization of ESG as an exam priority and key exam focus area, the establishment of its ESG Task Force, and the issuance of the Climate Risk Disclosure Rule and the ESG Disclosure Rule.

Does it Matter What Investors Think About ESG? (Nasdaq)

With much of the ESG debate taking place in the political arena, it remains prudent to incorporate analysis from individual investors and investment managers who are actually making the stock selections or asset allocations, rather than relying on politicians to reinterpret what fiduciary duty prohibits or requires in terms of ESG consideration.

State Legislature Initiatives

- **Alabama** passed SB 261, which prohibits the state from entering contracts with companies that engage in the economic boycott of activities related to fossil fuels or firearms. The law was effective as of September 1, 2023, and only applies to contracts entered into, on or after October 1, 2023.

- **Arkansas** passed SB 62, which prohibits any public entity from entering contracts with companies unless they certify in writing that they will not boycott energy, fossil fuels, firearms and ammunition industries. The law was effective as of August 1, 2023.

- **Idaho** passed HB 191, which prohibits any public entity from accepting or denying contracts based on ESG standards. The law was effective as of July 1, 2023.

- **Indiana** passed HB 1008, which prohibits state pension fund leaders from investing with firms that consider ESG principles, such as the failure to meet environmental standards or disclosures. The law was effective as of July 1, 2023.

- **Kansas** passed HB 2100, which prohibits any state agency from giving preferential or discriminatory treatment based on any ESG criteria when procuring contracts. The law was effective as of July 1, 2023.

- **Kentucky** passed HB 236, which requires pension fiduciaries to base investment decisions solely on pecuniary factors and prohibits consideration of nonpecuniary interests including ESG. The law was effective as of June 29, 2023.

- **North Carolina** passed HB 750, which prohibits any state agency from using ESG requirements to hire, fire or evaluate employees or in consideration of awarding state contracts or investment. The law was effective as of June 27, 2023.

- **Utah** passed SB 97, which prohibits a public entity from entering contracts with companies that engages in certain boycott actions against the energy, agricultural or firearms industries. The law was effective as of May 3, 2023.

Upcoming ESG Events

Responsible Business USA

Reuters
New York, NY
March 26-27, 2024

Earthx2024 Congress of Conferences

EarthX
Dallas, TX
April 22-26, 2024

Accelerating the Circular Economy

Sustainability Week US

GreenBiz
Chicago, IL
May 22-24, 2024

The Economist
New York, NY
June 12-13, 2024

Akin's ESG Practice

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Questions?

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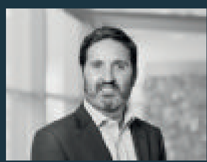

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