Fisher Broyles

CLIENT ALERT
April 26, 2021

BEYOND DISCLOSURE – THE EMERGENCE OF ESG AS A C-SUITE RISK FACTOR

PART II: NET-ZERO MOVEMENT GATHERS MOMENTUM[*]

The month of April 2021 has seen a flurry of significant international events with the common goal of elevating the urgency of the fight against climate change and committing to the fight in both public and private sectors. In a rare display of coordination across governments and global industries, governments and leading institutions committed to both internal and sector-wide transitions to a Net-Zero emissions economy, in accordance with the Paris Agreement[1] target of keeping global warming to 1.5 C above pre-industrial levels by the year 2050 ("Net-Zero").

United States Announces NDC

On Earth Day, April 22, 2021, President Biden announced that the United States will target a 50% - 52% reduction from 2005 levels in economy-wide net greenhouse gas ("GHG") pollution by 2030.[2] The announcement was made at the Leaders Summit on Climate, convened by President Biden and attended virtually by 40 world leaders, including the heads of state of the seventeen countries responsible for approximately 80% of global GHG emissions and global GDP.[3] The 2030 target constitutes the "successive nationally determined contributions" ("NDC") of the United States towards cutting GHG emissions and approximately doubles the United States' original NDC when it first signed on to the Paris Agreement in 2015.[4]

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[*] FisherBroyles is providing this alert as part of a series on ESG and its emergence as a risk factor for the C-Suite and legal, compliance, and risk professionals. This part of the series focuses on recent developments in international commitments to combat climate change, particularly in the financial sector, which are likely to provoke regulatory and policy shifts that will affect major segments of the global economy, including capital markets. The first part of the series can be found here. Future alerts will focus on other stakeholders as well as legislative initiatives.

[1] The Paris Agreement was adopted by 197 countries on December 12, 2015 at the 21st Conference of Parties (COP21) in Paris, France.

[2] FACT SHEET: President Biden Sets 2030 Greenhouse Gas Pollution Reduction Target Aimed at Creating Good-Paying Union Jobs and Securing U.S. Leadership on Clean Energy Technologies | The White House

[3] President Biden Invites 40 World Leaders to Leaders Summit on Climate | The White House The two-day Leaders Summit is a run-up to the 26th Conference of the Parties ("COP26") to the United Nations Framework Convention on Climate Change (the "UNFCCC") in Glasgow in November 2021.

[4] The Obama Administration originally committed to reducing GHG emissions by 26% - 28% of 2005 levels by 2025. Here's What the US Actually Agreed to in the Paris Climate Deal (businessinsider.com)

Europe Commits to Net-Zero Legally

At the Leaders' Summit, the European Commission announced a deal reached on April 21, 2021 for a new climate law that imposes binding targets on EU member states, including a 55% reduction in GHG emissions from 1990 levels by 2030. The landmark law also limits the amount of emissions removals that can be counted towards the 2030 target to 225 million tons of CO2 equivalent—e.g. reforestation and wetlands—thereby requiring that the target be met by cutting (rather than offsetting or compensating for) pollution.[5]

Other Major Commitments

At the Leaders Summit, Japan announced that it would almost double its current emissions target.[6] Canada announced a 40% - 45% reduction in emissions by 2030.[7] China reiterated its previous goal to reach carbon neutrality by 2060 and pledged to peak its coal consumption by 2025 and gradually reduce its coal reliance during its next five-year economic planning cycle.[8] Russia indicated its interest in international cooperation but did not appear to announce a concrete goal.[9]

Focus on Climate Financing

Separately from announcing its NDC, the United States also announced on April 22, 2021 a U.S. International Climate Finance Plan (the "Plan").[10] Climate financing refers to domestic or international finance that seeks to support mitigation of, and adaptation to, climate change. "Climate finance is needed for mitigation, because large-scale investments are required to significantly reduce emissions. Climate finance is equally important for adaptation, as significant financial resources are needed to adapt to the adverse effects and reduce the impacts of a changing climate."[11] The Plan refers to "climate finance" as "the provision or mobilization of financial resources to assist developing countries to reduce and/or avoid greenhouse gas emissions and build resilience and adapt to the impacts of climate change."[12] Among its initiatives, the Plan aims to:

- Double annual climate-related public finance to developing countries and triple its adaptation finance, both by 2024;
- Mobilize private financing internationally through U.S. agencies, such as expanding partnerships and blended finance to catalyze private capital for climate projects and supporting U.S. exports in renewables, energy storage, and energy efficiency. "U.S. agencies, including DFC,[13] U.S. Trade

[5] EU clinches deal on climate law, tougher 2030 emissions goal | Nasdaq
[6] Japan vows deeper emission cuts as Biden holds climate summit | Reuters
[7] Canada aims to almost halve its emissions by 2030 compared to 2005 levels - PM Trudeau | Reuters
[8] US pledges to double international climate finance at Earth Day summit (climatechangenews.com)
[9] The Latest: Putin seeks global cooperation on climate change | Markets Insider (businessinsider.com)
[10] EXECUTIVE SUMMARY: U.S. International Climate Finance Plan | The White House
[11] Introduction to Climate Finance | UNFCCC
[12] *Id*. The UNFCCC defines "climate finance" as "finance that aims at reducing emissions, and enhancing sinks of greenhouse gases and aims at reducing vulnerability of, and maintaining and increasing the resilience of, human and ecological systems to negative climate change impacts"
[13] The U.S. International Development Finance Corporation.

and Development Agency, EXIM,[14] the Department of State, MCC,[15] and USAID[16] will work together to build a strong investable project pipeline;"[17]

- Ending public financing of fossil fuel-based energy;[18]
- Making capital flows consistent with low-emissions, climate-resilient pathways, which includes continuing to "promote improving information on climate-related risks and opportunities; identifying climate-aligned investments; managing climate-related financial risks; and aligning portfolios and strategies with climate objectives."[19]
- Defining, measuring, and reporting U.S. international climate finance, including "more detailed reporting, tracking finance for vulnerable populations, and enhanced reporting on mobilization and impact."[20]

<u>The Glasgow Financial Alliance for Net-Zero</u>

On April 21, 2021, the United Nations and the United States launched the Glasgow Financial Alliance for Net-Zero ("GFANZ"), a global alliance of over 160 firms holding assets over $70 Trillion that will provide a single sector-wide strategic forum for net-zero initiatives.[21] "GFANZ will provide a forum for strategic coordination among the leadership of finance institutions from across the finance sector to accelerate the transition to a net zero economy."[22]

<u>The Net-Zero Banking Alliance</u>

Concurrently with the launch of GFANZ, the United Nations also convened the launch of the Net-Zero Banking Alliance ("NZBA"), an alliance of 43 banks from 23 countries with assets of $28.5 Trillion, whose members have committed to "align operational and attributable emissions from their portfolios with pathways to net-zero by 2050 or sooner."[23] NZBA member banks include Bank of America, Citi, Morgan Stanley, Barclays, Deutsche Bank, UBS, and HSBC.[24] Each member bank commits to:

- Transition the operational and attributable GHG emissions from their lending and investment portfolios to align with pathways to net-zero by 2050 or sooner;

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[14] The Export-Import Bank of the United States.
[15] The Millennium Challenge Corporation.
[16] U.S. Agency for International Development.
[17] *Supra* n. 10.
[18] *Id*.
[19] *Id*.
[20] Id.
[21] New Financial Alliance for Net Zero Emissions Launches | UNFCCC
[22] Id.
[23] Id. See also *infra* n. 26.
[24] Members – United Nations Environment – Finance Initiative (unepfi.org)

- Within 18 months of joining, set 2030 targets (or sooner) and a 2050 target, with intermediate targets to be set every 5 years from 2030 onwards. All targets will be regularly reviewed to ensure consistency with the latest science (as detailed in IPCC[25] assessment reports);
- Banks' first 2030 targets will focus on priority sectors where the bank can have the most significant impact—i.e. the most GHG-intensive sectors within their portfolios;
- Within 36 months of joining, banks will set a further round of sector-level targets for all or a significant majority of specified carbon-intensive sectors, including: agriculture; aluminum; cement; coal; commercial and residential real estate; iron & steel; oil & gas; power generation; transport;
- The commitment is designed to ensure that banks engage with their clients' own transition and decarbonization, promoting real economy transition rather than only financial sector withdrawal;
- Annually publish absolute emissions and emissions intensity in line with best practice and within a year of setting targets, disclose progress against a board-level reviewed transition strategy setting out proposed actions and climate-related sectoral policies; and
- Take a robust approach to the role of offsets in transition plans.[26]

The aforementioned commitments could have profound impacts on the specific industries mentioned above, particularly when one considers that the NZBA includes some of the world's largest financiers of those industries.

NZBA joints two existing alliances: the Net Zero Asset Managers Initiative, whose 87 members represent $37 Trillion,[27] and the Net-Zero Owner Alliance, a group of 37 institutional investors representing $5.7 Trillion in assets under management.[28] Yet another alliance is expected to be convened by the United Nations: the Net-Zero Insurance Alliance, founded by seven leading insurance companies.[29]

Conclusion

The Leaders Summit on Climate marked an important milestone towards COP26.[30] The urgency of the need to enact significant cuts in GHG emissions this decade was made plain by world leaders. It was also clear from the Leaders Summit that climate change transcends all other political and economic differences among nations and that leadership by the United States is both necessary and welcomed by the world community.

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[25] IPCC — Intergovernmental Panel on Climate Change
[26] 43 banks launch Net-Zero Banking Alliance as key part of consolidated Glasgow COP climate action – United Nations Environment – Finance Initiative (unepfi.org)
[27] State Street Global Advisors Joins Net Zero Asset Managers Initiative - ESG Today
[28] United Nations-Convened Net-Zero Asset Owner Alliance – United Nations Environment – Finance Initiative (unepfi.org)
[29] UN-convened Net-Zero Insurance Alliance – United Nations Environment – Finance Initiative (unepfi.org)
[30] *Supra* n. 3

However, much of the United States' NDC will require legislative action in order to be implemented and will therefore be subject to Congressional approval, which is not guaranteed. The American Jobs Plan proposed by President Biden seeks to inject over $2 Trillion into the U.S. economy, approximately half of which is earmarked for the transition to a low-carbon economy with two primary objectives: de-carbonizing electricity production by 2035 and transitioning the automobile industry towards producing electric vehicles only.[31] Also, the American Jobs Plan does not include carbon pricing,[32] which many leaders at the Leaders Summit evoked as essential to phasing out fossil fuels.

These developments reinforce the regulatory changes regarding ESG disclosures currently underway within the U.S. Securities and Exchange Commission and in global capital markets more broadly. While proposed legislation makes its way through Congress, private industry appears ready to not only follow but lead on the transition to Net-Zero and other ESG issues, by recognizing and committing to combatting climate change in an unprecedented manner. While it remains to be seen what specific laws and regulations will be enacted, the clear take-away of the Leaders Summit and the launch of the GFANZ, NZBA and other important alliances is that change is coming to major sectors of the global economy, and industrial players and market participants should closely monitor and anticipate the impacts of these changes where appropriate.

FisherBroyles will continue to report on important developments concerning ESG matters and their potential effects on publicly traded companies, the capital markets, and on other industries likely to be affected. We are able to advise and assist you with SEC disclosure matters as well as both proactive efforts to build and maintain a risk and/or compliance program, as well as responding to regulatory inquiries and enforcement matters.

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[31] FACT SHEET: The American Jobs Plan | The White House
[32] The two main forms of carbon pricing are emissions trading systems (also referred to as "cap-and-trade") and carbon taxes. Both have the effect of shifting the burden for the damage done by carbon emissions to those who are responsible for it. "Instead of dictating who should reduce emissions where and how, a carbon price gives an economic signal and polluters decide for themselves whether to discontinue their polluting activity, reduce emissions, or continue polluting and pay for it." Pricing Carbon (worldbank.org)