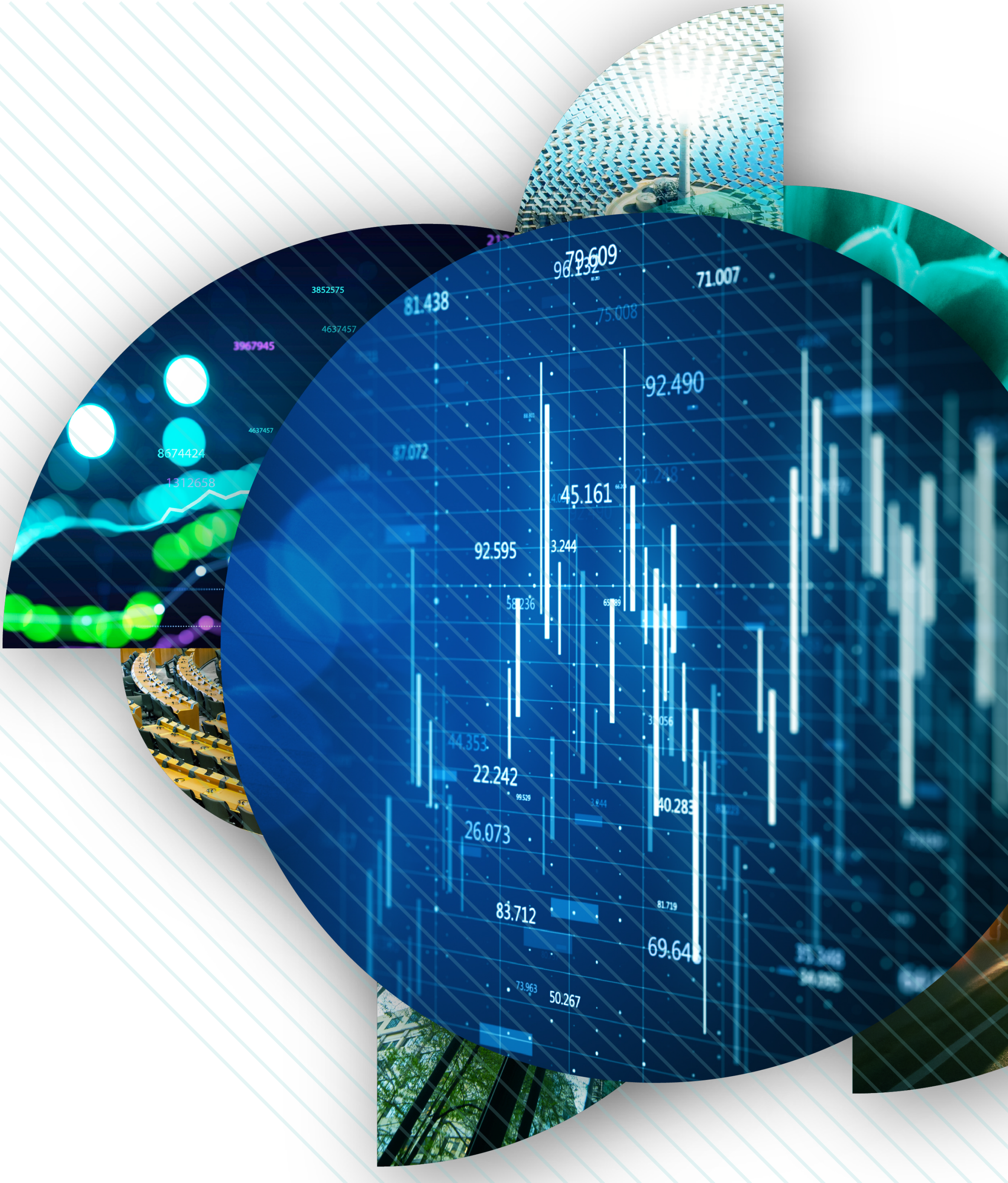
NORTON ROSE FULBRIGHT

ESG | Sustainability

Financial Services regulatory ESG updater

10 September – 6 October 2024



Introduction

Environmental, Social and Governance (ESG) is changing the landscape for financial institutions as a wide range of stakeholders including investors increasingly expect them to make their operations more sustainable. Financial services regulators also view ESG as a priority, embedding the principles of climate-related financial risks into their supervisory frameworks and dealing with institutions that may be making exaggerated or unsubstantiated sustainability-related claims that do not stand up to closer scrutiny (so-called 'greenwashing'). However, the key problem for institutions, particularly those operating cross border, is that there is limited uniformity in regulation, financial services regulators are at different stages in developing their ESG regulatory framework particularly in relation to disclosures and taxonomy. It is therefore critical that institutions monitor the latest announcements from the regulators.

The purpose of this updater is to track ESG regulatory developments from the period September 10, 2024 to October 6, 2024, from the United Kingdom, France, Europe Union, the Netherlands, United States, Australia, and certain international regulators.

This month's highlights

September 11, 2024 - Let's talk asset management: Episode 5 – Updated Q&As on SFDR: key issues for fund managers

In the latest episode of our podcast series, Let's talk asset management, Cédric Danois and Simon Lovegrove discuss some of the key issues that ESMA and the other ESAs raise in the updated Q&As on the SFDR:

- Sustainable investment definition
- Website disclosures
- Principal adverse impact indicators

Listen to the episode here.

United Kingdom

September 27, 2024 - DESNZ note on extending the UK ETS first Free Allocation period to 2026

The Department for Energy Security and Net Zero updated it's webpage on the UK Emissions Trading Scheme (**UK ETS**): free allocation review by adding a note on extending the UK ETS first Free Allocation period to 2026. The note states that the UK ETS Authority is consulting operators in the scheme on a proposal to move the start of the second allocation period from 2026 to 2027, extending the current allocation period to include 2026. Operators will receive the consultation from their scheme regulator and have until October 11 to submit responses. The change is designed to align changes to Free Allocation with the introduction of the UK Carbon Border Adjustment Mechanism in 2027. The UK ETS Authority is also proposing that:

- The baseline data reporting exercise will continue as planned from April 1 to June 30, 2025.
- Applications for the second free allocation period will be made in 2026.
- Updated lists of installations with hospital or small emitter (**HSE**) and ultra-small emitter (**USE**) status will come into effect from 2026, with the application window for inclusion on these lists open from April 1 to June 30, 2025.
- Changes to the current rules regarding the electricity generator classification will come into effect in 2026.

European Union

There have been no reported updates this month.

France

There have been no reported updates this month.

The Netherlands

October 3, 2024 – DNB Working Paper: Green transition in the Euro area – Domestic and Global Factors

The Dutch Central Bank (**DNB**) published a Working Paper, Green transition in the Euro – Domestic and Global Factors.

The Working Paper analyses the macroeconomic implications of climate-related policies aimed at promoting the switch to green energy, with a specific focus on carbon taxes and green subsidies as well as on taxes on brown investment and subsidies for green investment. In particular, it uses the Euro Area and Global Economy (**EAGLE**) model, a dynamic stochastic general equilibrium model representing the Euro Area within the global economy.

Among other things, the Working Paper highlights the following:

- A carbon tax has effects similar to those of an adverse cost-push shock. Without subsidies to green energy firms, the green transition is limited to household expenditure switching towards green energy goods.
- Subsidies to green energy firms lead to a lower price of green energy and boost the intermediate good sector's demand for green energy inputs.
- When carbon taxes are raised globally, the recession in the Euro area deepens while inflationary pressures amplify, triggered partly by a weakening of the euro.

United States- SEC and CFTC

September 19, 2024 – CFTC issues guidance regarding the listing of voluntary carbon credit derivative contracts

The Commodity Futures Trading Commission (**CFTC**) issued guidance to outline the factors for consideration by designated contract markets, when addressing certain provisions of the Commodity Exchange Act and CFTC regulations thereunder, that are relevant to the listing for trading of voluntary carbon credit (**VCC**) derivative contracts.

The guidance also outlines factors for consideration when addressing certain requirements under the CFTC's Part 40 regulations that relate to the submission of new derivative contracts and contract amendments to the CFTC.

October 2, 2024 – CFTC charges former CEO of carbon credit project developer with fraud involving Voluntary Carbon Credits

The CFTC filed a complaint in the U.S District Court for the Southern District of New York against Kenneth Newcombe of California, the former Chief Executive Officer and majority shareholder of a Washington D.C based carbon credit project developer, charging fraud and false, misleading, or inaccurate reports relating to VCCs.

The CFTC also issued orders filing and settling charges against Washington D.C based CQC Impact Investors LLC (**CQC**) and against Jason Steele, CQC's former Chief Operating Officer. These are the first CFTC actions for fraud in the VCC market.

Australia

September 9, 2024 - Climate-related financial disclosure regime becomes law

The Australian Parliament passed the *Treasury Laws Amendment (Financial Market Infrastructure and Other Measures) Act 2024* (Cth) (the **Act**) on September 9, 2024.

The Act establishes Australia's climate-related financial disclosure (**CRFD**) regime, requiring entities that meet certain size thresholds to disclose their climate-related risks, opportunities, and control mechanisms as part of a mandated annual sustainability report.

The Act will be enforced in three phases with Group 1 entities, that are entities that meet two out of three of the following criteria, being required to report from January 1, 2025:

- consolidated revenue of $500 million or more;
- consolidated gross assets of $1 billion or more; and/or
- more than 500 employees.

Group 1 entities also include entities that are already National Greenhouse and Energy Reporting (**NGER**) Reporters.

Smaller entities in Group 2 and 3 will be required to report from July 1, 2026 and July 1, 2027 respectively.

September 17, 2024 - Audit and Assurance of Sustainability Reports

The Australian Auditing and Assurance Standards Board (**AUASB**) published an Exposure Draft of a Proposed Australian Standard on Sustainability Assurance (ASSA 5010) that outlines a proposed timeline for when information in a sustainability report prepared in accordance with the CRFD would be subject to audit and/or review.

The AUASB proposes the following levels of assurance:

- limited assurance over Scope 1 and 2 emissions from the first year of reporting, progressing to reasonable assurance in the second year of reporting;
- limited assurance over governance and strategy (risks and opportunities) from the first year of reporting, progressing to reasonable assurance in the fourth year of reporting; and
- limited assurance over all other disclosures from the second year of reporting, progressing to reasonable assurance in the fourth year of reporting.

The Exposure Draft was developed based on feedback that assurance should begin with limited assurance for a period of time before progressing to reasonable assurance as the previously proposed timeline was too ambitious.

AUASB is seeking comments and feedback on the Exposure Draft by November 16, 2024. The proposed standards will be operative from January 1, 2025 to June 30, 2030.

September 25, 2024 - Vanguard ordered to pay $12.9 million penalty for greenwashing

The Federal Court of Australia has ordered Vanguard Investments Australia to pay a record $12.9 million penalty for making misleading claims about environmental, social and governance (**ESG**) exclusionary screens. The penalty was ordered in relation to successful greenwashing proceedings commenced by Australian Securities and Investments Commission (**ASIC**) in which the Federal Court, in March of this year, found that the global investment company had made false and misleading statements in representing that certain ESG exclusionary screens applied to investments in its 'Ethically Conscious Global Aggregate Bond Index Fund (Hedged)' (**Fund**).

In ordering the aggregate $12.9 million penalty, the Federal Court considered the seriousness of the contravening conduct, the length of the contravention period spanning two and a half years, the substantial size of the fund and the seniority of employees involved in the contraventions. The Federal Court made clear that Vanguard's contraventions "should be regarded as serious" and there was a "reckless disregard to the accuracy of information conveyed". Further, the Court observed that "[t]he desire to promote and market the Fund as "ethically conscious" took priority over ensuring that the composition of the Fund, and the extent of ESG screening, were accurately disclosed".

However, in accepting Vanguard's submission that it should receive a 25 per cent discount, the Federal Court had regard to its cooperation with ASIC in its investigation and the steps it had since taken to improve its compliance procedures to avoid future greenwashing.

International regulators – FSB, IOSCO, Basel Committee, NGFS, SASB, IFRS, ISSB

There have been no reported updates this month.

Resources

ESG is high on the regulatory agenda. Businesses, governments, regulators, financial services firms and individuals all have a part to play in tackling climate change and this view is increasingly shared across society. In terms of financial markets, investors are increasingly seeking sustainable financial products and ESG investing, traditional investing combined with sustainable or otherwise philanthropic aims, has seen huge growth in recent years. Regulated firms are also seeking to improve their own ESG performance more generally to build stronger relationships with their stakeholders, including those who use their services. Whilst the growing emphasis on ESG presents opportunities for financial services providers, it also brings with it a number of risks, which need to be properly managed with a view to avoiding future regulatory investigations and enforcement.

We have produced a number of resources, including articles, podcasts and newsletters, to help clients navigate this evolving, complex landscape:

Financial services: Regulation tomorrow

Our blog, Financial services: Regulation tomorrow offers a convenient resource for those keeping track of the evolving and increasingly complex global financial services regulatory environment.

Financial Services Regulatory Developments in ESG

Developed by our global financial services regulatory lawyers and integrated risk advisory group, our Financial Services Regulatory Developments in ESG Hub provides resources and insights to help clients stay informed of key regulatory developments in the sector.

ESG and Sustainability Insights newsletter

Our ESG and Sustainability Insights newsletter brings together recent insights and resources on key topics affecting your business, including climate change and regulation, business and human rights, sustainable finance, energy transition and more.

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