

Five Key ESG Developments: How to Prepare in 2024

February 2024

Agenda

- California Climate Accountability Package
- EU Corporate Sustainability Reporting Directive
- SEC forthcoming climate disclosure rules
- Diversity, equity and inclusion
- Supply chain rulemaking

Presenters



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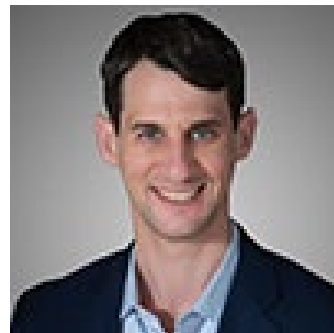
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California Climate Accountability Package

- Three new California laws enacted October 2023, of far-reaching applicability and scope; similar bills under consideration in NY, Illinois
 - Governor Newsom expressed concerns upon signing SB 253 and SB 261, including around feasibility of implementation deadlines
 - US Chamber of Commerce filed suit in late January 2024 in federal court seeking to invalidate two of the new laws – SB 253 and SB 261 – on grounds of First Amendment violation, federal law preemption (Clean Air Act) and Dormant Commerce Clause violation (extra-territorial application)
- Climate Corporate Data Accountability Act (SB 253)
 - Applies to US entities with total annual revenues exceeding \$1 billion that do business in California -- including private companies, LLCs and partnerships
 - From 2026, requires disclosure of annual scope 1 and scope 2 greenhouse gas (GHG) emissions
 - From 2027, requires disclosure of annual scope 3 GHG emissions
 - Disclosures to be verified by an independent auditor (phased, starting with limited assurance in 2026)

California Climate Accountability Package

- Climate-Related Financial Risk Act (SB 261)
 - Applies to US entities with total annual revenues exceeding \$500 million that do business in California -- including private companies, LLCs and partnerships
 - Requires annual report disclosing the entity's climate-related financial risk and measures adopted to reduce and adapt to climate-related financial risk
- Voluntary Carbon Market Disclosures (AB 1305)
 - Applies to businesses operating in California that market or sell voluntary carbon offsets, or make claims regarding the achievement of net zero emissions, carbon neutral status about the company or a product, or significant carbon emissions reductions
 - Requires website disclosure regarding these activities including whether data and claims have been verified by an independent third-party; targets greenwashing
 - Effective January 1, 2024 but California legislature asked to extend in line with bill author's intentions; many companies have already provided this disclosure

California Climate Accountability Package

- AB 1305 requires companies operating in California to disclose backup detail regarding “carbon neutral” and “net zero” claims

Requirements for Entities Making Emissions Claims

All businesses operating in California making “carbon neutral,” “net zero emissions”, or other similar emissions claims must disclose on its website:

- All information documenting how the claim was determined to be accurate or accomplished, or how interim progress toward the goal is being measured (including both the underlying data and methodology used to support the claim)
- Whether there is independent third-party verification of the company data and claims listed

Requirements for Entities Using Offsets to Make Emissions Claims

Companies using voluntary carbon offsets as a part of their environmental claims must additionally disclose:

- The business entity selling the offset and the offset registry or program
- The project name and project identification number, if applicable
- The offset project type, including whether the offsets were derived from carbon removal, avoided emissions, or a combination of both
- The project site location
- The specific protocol used to estimate removal benefits and/or emission reductions
- Whether an independent third party has verified the underlying data and claim

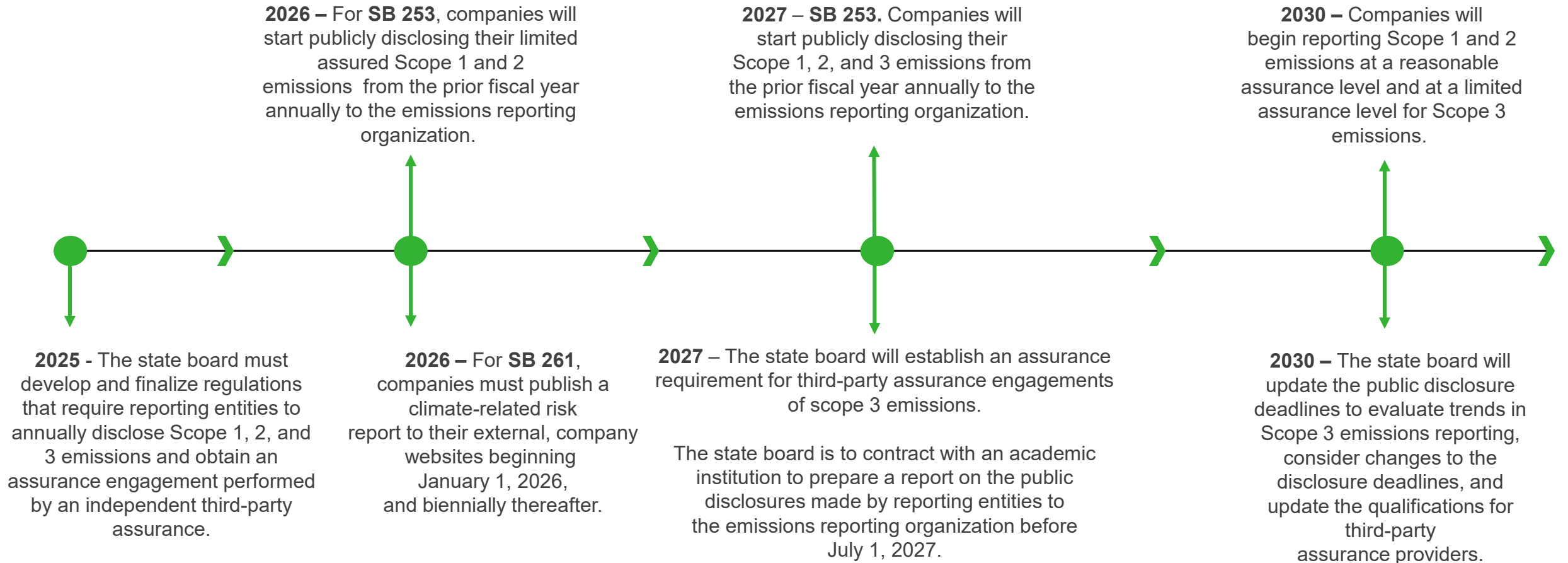
Requirements for Marketers and Sellers of Offsets

Businesses marketing or selling voluntary carbon offsets within the state must disclose:

- The project type, site location, start date, timeline, and durability period
- The specific protocol used to estimate removal benefits and/or reductions
- Carbon removed or emissions reduced on an annual basis
- The durability period of the project
- Whether the project meets any standards established by law or by a nonprofit entity
- Whether an independent third party has validated or verified the project attributes

California Climate Accountability Package

Timeline of disclosure and assurance requirements of SB 253 and SB 261



EU Corporate Sustainability Reporting Directive

- CSRD in force since January 2023, amending several EU directives, to expand sustainability reporting requirements and capture businesses doing significant business in the EU; sustainability reporting subject to independent assurance
 - Requires implementation by each EU country
- European Sustainability Reporting Standards (ESRS) promulgated by EFRAG under CSRD; Q&A portal and non-binding implementation guidance also available
 - Cross-cutting ESRS include general reporting concepts and data points
 - Ten topical ESRS covering ESG topics, including data points
 - Environmental (5 ESRS)
 - Social (4 ESRS)
 - Governance (1 ESRS)
 - Under development: sector-specific ESRS and ESRS for non-EU companies

Sustainability Topics to be Considered

Environmental

- » Climate change
- » Pollution
- » Water and marine resources
- » Biodiversity and ecosystems
- » Resource use and circular economy

Social

- » Own workforce
- » Workers in the value chain
- » Affected communities
- » Consumers and end-users

Governance

- » Business conduct

CSRD provides this list of topics as guidance, but companies still need to consider their own specific circumstances when determining their material matters.

EU Corporate Sustainability Reporting Directive

CSRD applies to:

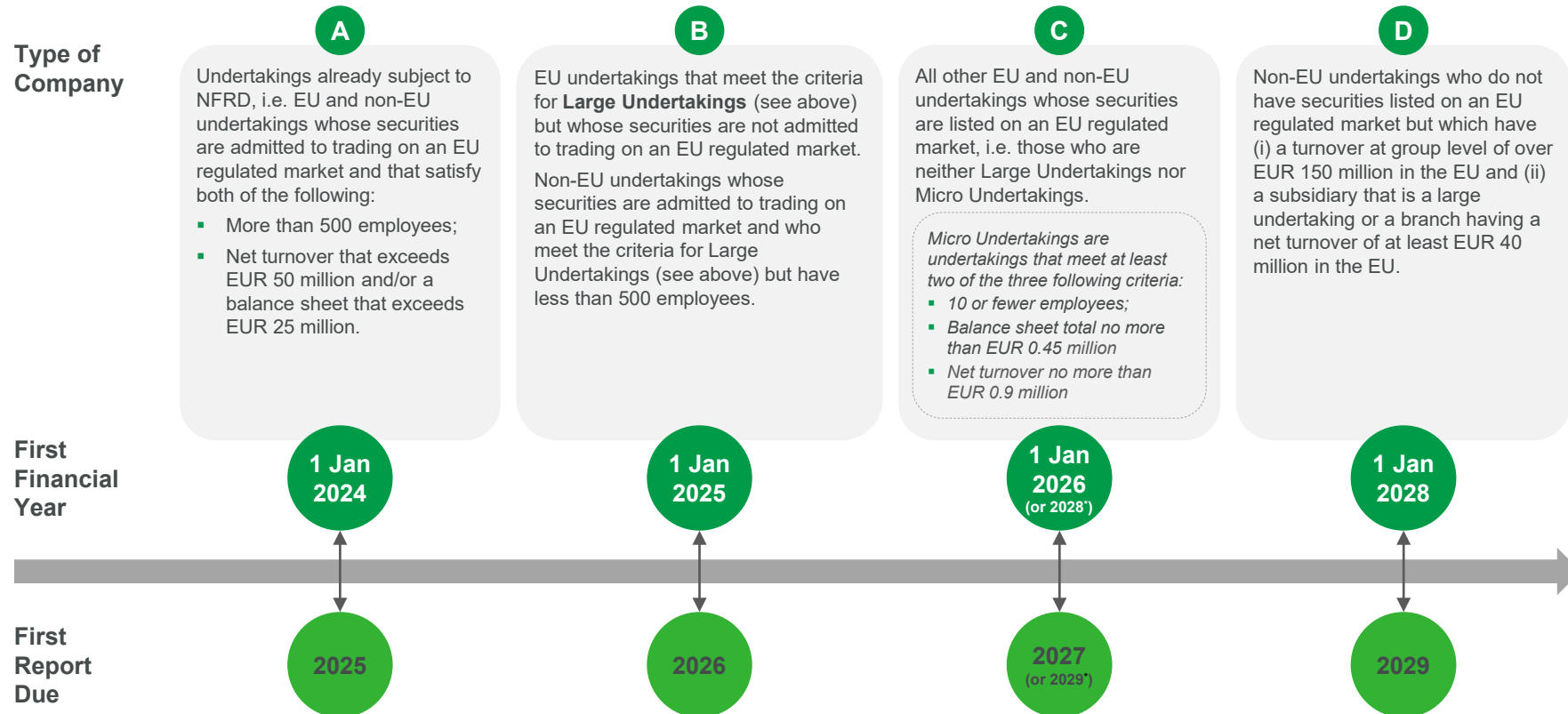
- 1** A “**Large Undertaking**”: a undertaking incorporated in the EU (an “**EU Undertaking**”) that meets at least two of the three following criteria on its balance sheet date:
 - Balance sheet total: EUR 25 million
 - Net turnover: EUR 50 million
 - Average number of employees during the financial year: 250
- 2** A “**Public-Interest Undertaking**”: an EU Undertaking that is either:
 - (i) listed on a regulated EU stock market;
 - (ii) a specific form of financial services company (e.g. insurance company or credit institution); or
 - (iii) an undertaking specifically designated as a public interest entity in its country of incorporation
- 3** A “**Non-EU Undertaking with Significant Presence in the EU**”: an undertaking not incorporated in the EU that has generated a net turnover within the EU of EUR 150 million for two consecutive financial years, and also meets at least one of the following criteria:
 - Has a subsidiary in the EU that meets the thresholds mentioned in 1 or 2; or
 - Has a branch in the EU that generated EUR 40 million net turnover in the preceding financial year.
- 4** A “**Parent of a Large EU Group**”: EU Undertakings that are parents of groups of undertakings that meet the thresholds mentioned in 1.

The reporting obligations applicable to in-scope undertakings will vary depending on the type of undertaking and the specific ESRS that will apply

EU Corporate Sustainability Reporting Directive

- Several ESRS focus on the provision of data, covering greenhouse gas emissions, energy, water, waste, recycling and social metrics
- Undertakings will be required through the ESRS to digitally tag reported information, in order to allow the information to be located, machine-readable and easily comparable
- Undertakings will be subject to reporting on double materiality for certain ESRS, ensuring that the relevant ESRS disclosure focuses both on the impact to the undertaking (financial materiality) and to the wider community where this does not necessarily impact the undertaking directly (impact materiality)
 - Expected to lead to a change in companies' understanding of risk and a review of risk assessment processes
- Undertakings must report not only on their own operations but also the broader value chain (i.e. material impacts, risks and opportunities connected to the undertaking through its direct and indirect business relationships)
 - Value chain obligation applies both upstream and downstream from the relevant undertaking
 - Where an undertaking is unable to obtain this information, for the first three years of application of CSRD, the undertaking will be permitted to instead explain the reasons for this and set out the efforts intended to be made to obtain the required information on a go-forward basis

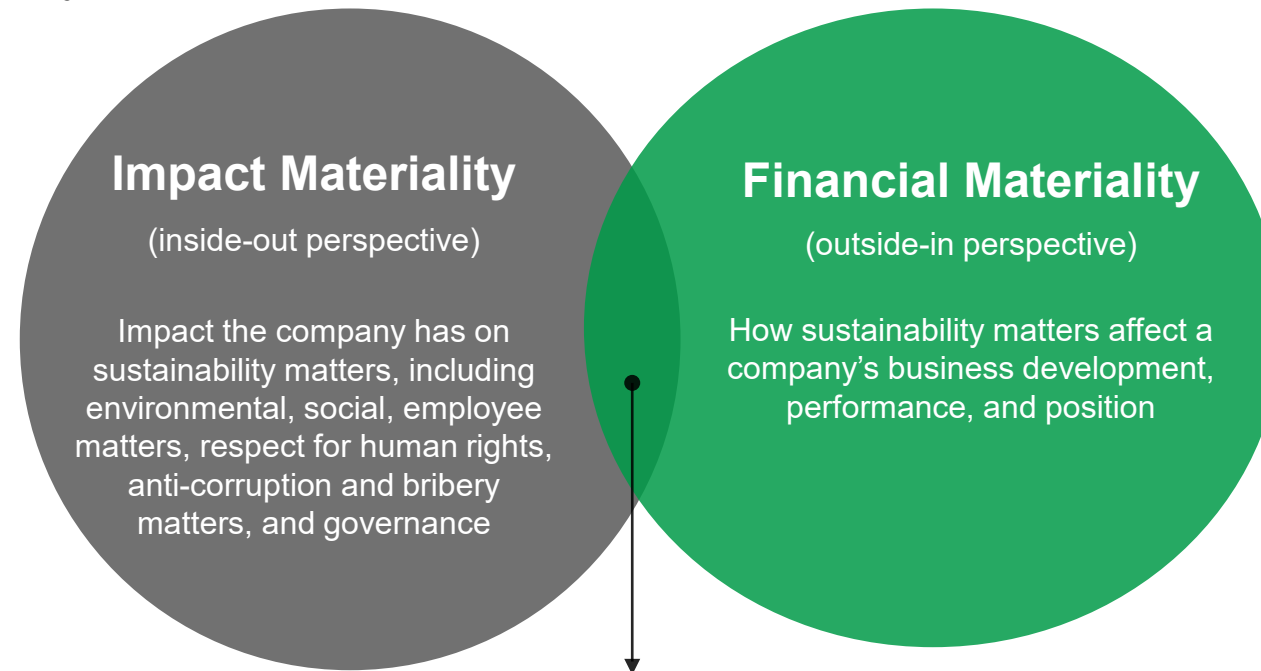
EU Corporate Sustainability Reporting Directive



* For a transitional period of two years, small and medium sized EU and non-EU undertakings with securities on an EU regulated market have the possibility to opt-out from CSRD reporting requirements, provided that they briefly explain in their management report why the required sustainability information has not been included.

EU Corporate Sustainability Reporting Directive: Double Materiality Assessment

- Under CSRD, companies must conduct a double materiality assessment to identify which sustainability matters are most material to the organization and its stakeholders, which will inform their reporting requirements
- Companies need to consider each materiality perspective in its own right
- A sustainability matter may be material from an impact perspective, a financial perspective, or both



For example, if a company in agriculture depletes land of a field (inside-out impact), this could directly affect the yield of crops and ultimately the financial margin of the company (outside-in effect)

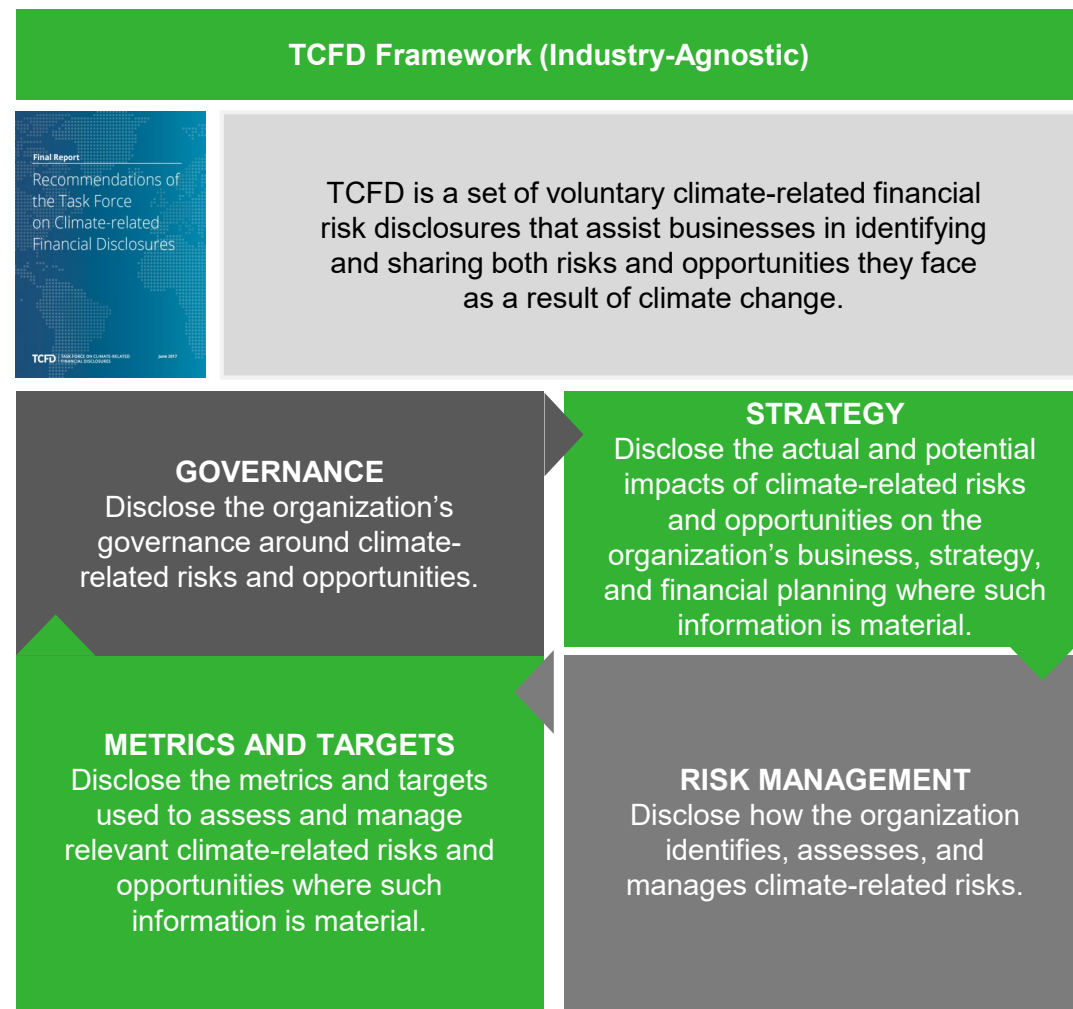
SEC Climate Disclosure Rulemaking

- SEC is yet to adopt final rules on climate change disclosure
 - Proposed rules would require disclosure of Scope 1 and 2 emissions, and Scope 3 emissions if material or if the company has set a GHG emissions target or goal that includes Scope 3 emissions, as well as disclosures around climate-related risks and related oversight, and financial statement metrics
 - Independent third-party assurance would be required for certain disclosures
 - Would also apply to foreign private issuers
- Significant international developments around climate change disclosure since rules proposed in March 2022; well over 10,000 comments received, including much scrutiny over Scope 3 disclosure requirement
 - Unified Regulatory Agenda indicates final rules in April 2024 but no guarantee that will occur
- SEC reviews all climate-related disclosures and has issued comments when ESG report disclosures are more expansive than SEC filing disclosures

SEC Climate Disclosure Rulemaking

- US and global requirements are aligned closely with TCFD disclosure recommendations

Select SEC CDR Topic Areas	In TCFD?
Board oversight of climate-related risks	✓
Management’s role in assessing and managing climate-related risks	✓
Discuss climate-related risks and identify which risks are physical and transition risks, as well as the risks’ time horizon	✓
Describe the actual and potential impact of the defined climate-related risks, including the potential impact on the registrant’s consolidated financial statements	SEC More Prescriptive
Describe the resilience of the business’ strategy, including any scenario analysis used	✓
Describe processes for identifying, assessing and managing climate-related risks and how that is integrated into overall risk management	✓
Disclose Scope 1 and 2 emissions	✓
Disclose Scope 3 emissions if material or if a reduction target goal has been set	SEC More Prescriptive
Disclose targets or goals related to emissions or climate-related concerns if one has been set	✓
Disclose impact on financial statements, including the impact of severe weather events, efforts or expenditures to reduce emissions, and key transition activities	SEC More Prescriptive



Diversity, Equity & Inclusion

- Corporate DEI programs under scrutiny, particularly since US Supreme Court decision in SFFA v. Harvard (June 2023) relating to college admissions programs -- not in employment decision context (Title VII)
 - Court held that giving preferential weight to members of certain racial minorities are unconstitutional, because race-based classifications not justified (applying strict scrutiny standard)
- Examples of DEI backlash:
 - Letters to companies sent by Republican members of Congress
 - Lawsuits against law firms offering diversity scholarships
 - Shareholder proposals targeting supplier diversity programs
 - Challenge to Nasdaq board diversity rule; dismissal overturned by Court of Appeals for the Fifth Circuit and will be reheard
- Companies focused on strategic importance of DEI and reviewing DEI-related disclosure in light of expectations of investors, employees, suppliers, etc.

Diversity, Equity & Inclusion

- Despite recent and significant noise regarding DEI, shareholder expectations and issuer disclosure are more closely aligned

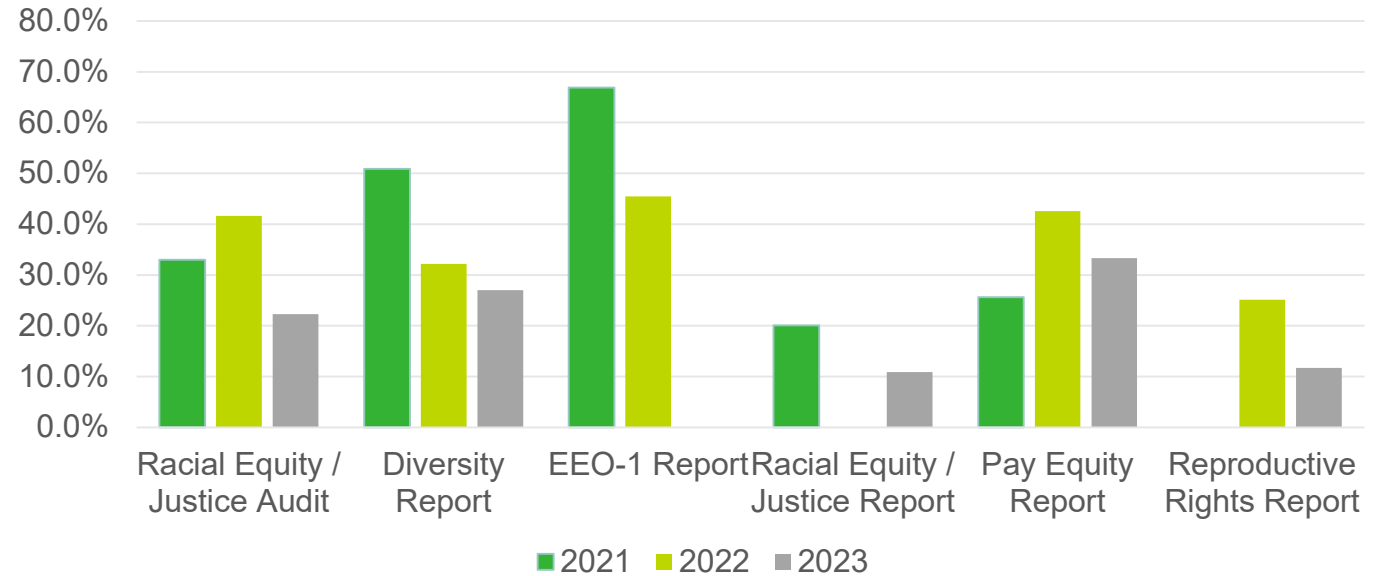
Investment Stewardship Expectations

- Core expectations for issuer action on DEI topics have not materially changed in recent years and in some instances are stronger – e.g., board gender diversity
- Engagement, coordinated with updated disclosure, remains critical on DEI practices and human capital strategies – and are evolving further – e.g., human rights, employee rights
- Pushback from self-proclaimed “anti-ESG” proponents has led to numerous contrarian shareholder proposals focused on diversity, though support remains extremely limited

Company Disclosures

- Issuer transparency on DEI initiatives continues; investor expectations have encouraged some issuers to be more open to additional transparency to withdraw a proposal
- Word choice and refinement is expected, target setting is likely to slow

Support on Diversity-Related Shareholder Proposals*



* Averages exclude proposals submitted by “anti-ESG” proponents which have received minimal support.

Supply Chain Rulemaking

- Significant developments relating to supply chain diligence that need to be factored into supplier management processes, including increased focus on human rights and the environment
 - EU Corporate Sustainability Due Diligence Directive under development
 - Supplier diligence laws enacted in several EU countries (including France, Germany, Netherlands)
 - Updated OECD Responsible Business Conduct Guidelines
 - US federal government rulemaking
 - Federal Supplier Climate Risk and Resilience Rule
 - Federal Sustainable Products and Services procurement rule
- Wide range of topics relevant to supply chain including environmental impact, working conditions, safety, modern slavery/child labor, materials from conflict regions, technology/data, sanctions and bribery
- Supply chain also impacted by Scope 3 reporting requirements under CSRD, California SB 253 and other regulations

Supply Chain Rulemaking: CSDDD

- Eligibility requirements and timeline; likely multiplier effect for small and medium enterprises

EU Companies

EU companies/ultimate parent companies with at least 1000+ employees and net €300 million turnover

EU companies with 500+ employees and net €150+ million turnover

EU companies with royalties of net €7.5+ million turnover

EU ultimate parent companies with net €40+ million turnover

EU companies with 250+ employees, net €40+ million annual turnover with net €20+ million annual turnover from high-risk sectors

If legislation passes in

FY 2024

FY 2027

FY 2028

FY 2029

Non-EU Companies

Non-EU companies/ultimate parent companies with net annual turnover of over €150 million from within the EU

Non-EU companies with royalties of net €7.5+ million turnover in the EU

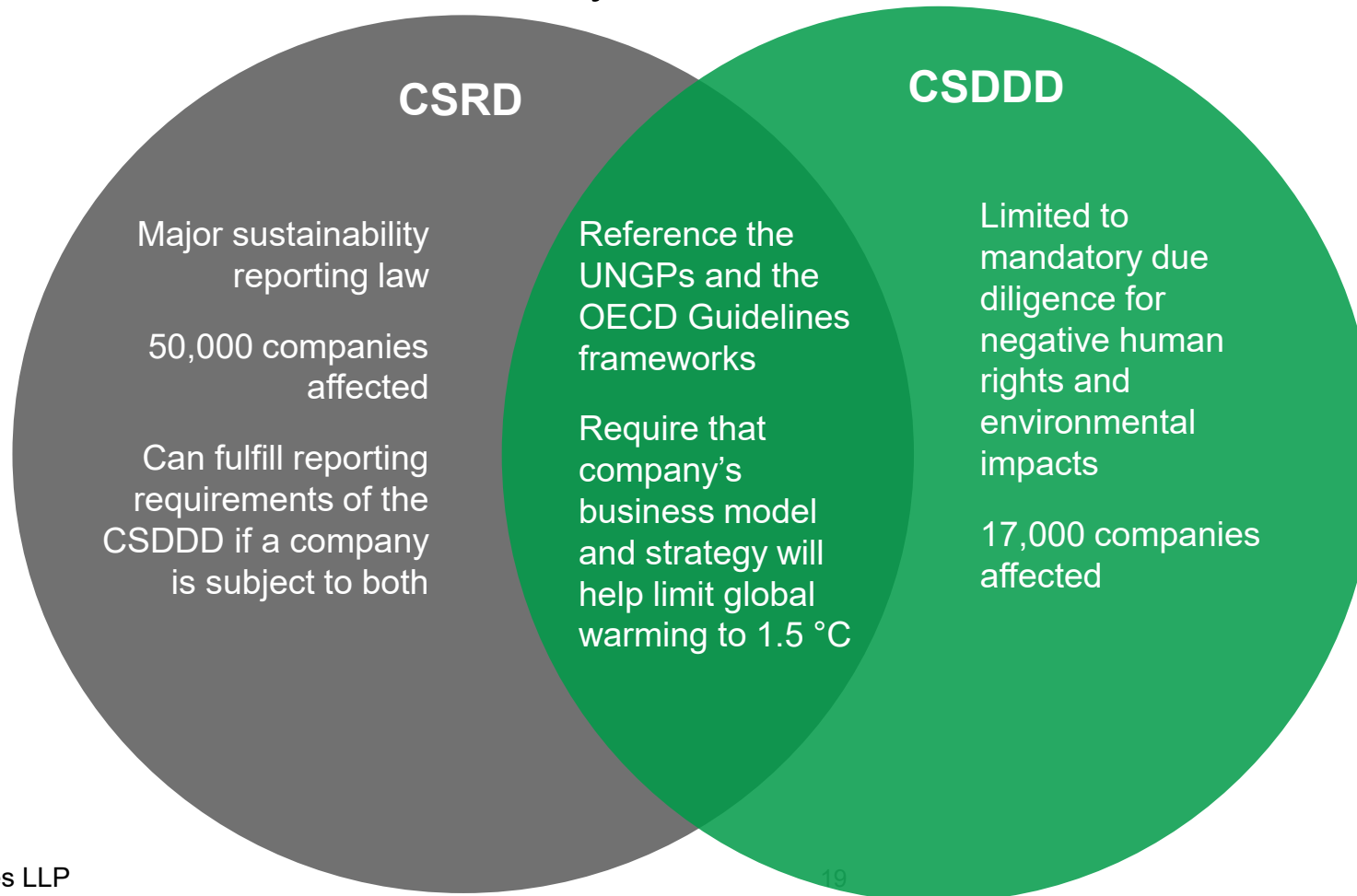
Non-EU ultimate parent companies with net €40+ million turnover from within the EU

Non-EU companies with net €40+ million annual turnover with net €20+ million annual turnover from high-risk sectors

- Compliance mechanisms
 - Administrative liability
 - Non-compliant companies will face penalties including “naming and shaming” and, reportedly, fines of up to 5% net turnover
 - Civil liability
 - Companies can be held liable for the damage caused by breaching their due diligence obligations
 - Impacted persons and their representatives (potentially including trade unions and civil society organizations) will have a five-year window to lodge damages claims
- CSDDD is not final
 - The agreement will be voted on in a straight up or down vote, without amendment
 - The European Council and European Parliament’s Committee on Legal Affairs (JURI) vote was postponed when Germany, Italy, and Finland indicated that they would abstain from the vote. A new date for the vote has not been set
 - Following approval by JURI, the full Parliament will vote

CSRD & CSDDD

- CSRD and CSDDD are complementary in that they aim to help the EU to achieve its net-zero goals and build a more sustainable economy



Next Steps

- Assess ESG disclosure regulations to pre-empt strategic impact and disclosure demands
- Conduct a gap analysis against forthcoming regulations to identify what data is being gathered and what data will need to be gathered, and implement processes to ensure disclosures will be assurance-ready
- Review disclosure controls and procedures to ensure that sustainability disclosures are appropriately covered
- Conduct a health check of disclosures and marketing claims, to identify risks of greenwashing accusations
- Undergo a double materiality assessment if CSRD applies
- Review DEI programs for potential vulnerabilities
- Review your supply chain and increase collaboration with suppliers to reduce value chain risk where possible (e.g., relating to climate, human rights, etc.)