

ENVIRONMENTAL, SOCIAL & GOVERNANCE

Law Over Borders Comparative Guide 2023

Edited by Ulysses Smith, Debevoise & Plimpton LLP

THE
GLOBAL LEGAL POST

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ESG IN 2023: A FRAGMENTING LANDSCAPE

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It is a dynamic time for ESG globally, especially in the United States.

At the macro level, various developments are challenging the customary ESG narrative. That narrative has been one of ever-increasing ESG commitments by the business community. This ambition has included embedding and operationalizing environmental, social, and governance considerations in corporate strategies, making net zero commitments, and speaking out against injustices or threats to democratic governance. In the meantime, companies must continue to be profitable enterprises and generate returns for shareholders.

The narrative, simply put, could be described as “win-win,” as “having your cake and eating it too,” when it comes to profitability and conducting your business responsibly.

That narrative has shifted dramatically over the last year, driven in part by the energy crisis and the war in Ukraine. Macroeconomic developments have made ESG seem more expensive to pursue, and the political environment (especially in the United States) seemingly has subsumed the broader ESG conversation. This past year saw calls for the end of ESG, highlighting flaws in certain ratings methodologies or suggesting disbanding ESG terminology. One notable executive referred to ESG as “satanic.”

On the other hand, an array of data suggests that realities underlying the ESG narrative — climate change and biodiversity loss, racial injustice, and the corrosive effects of poor governance — have never been more dire. Talk of the “future of ESG” can seem to be little more than a sideshow. The recent impacts of climate change are unmistakable, including horrific floods in Pakistan, massive droughts and forest fires in the western U.S., and deadly heat waves in Europe. These challenges have kept the focus on climate and broader “E” issues, as witnessed in the recent COP27 meetings in Egypt, and COP15, the UN’s biodiversity summit, in Canada.

The Inflation Reduction Act, the most significant climate legislation in U.S. history — notwithstanding the misnomer — is expected to transform the decarbonization of the U.S. economy and the transition to clean energy. It includes significant tax incentives for electric vehicles and related infrastructure, resources to help citizens decarbonize their homes and places of work, and the creation of a “green bank” to help draw in private capital into climate friendly investments. This development stands in stark contrast to much of the “anti-ESG” pushback we’ve seen.

In addition, the U.S. midterm elections played out differently from what many expected and will seemingly allow the Biden Administration to continue advancing its green agenda. It also may serve to limit how far Republicans can advance certain congressional initiatives, including opening investigations into the ESG commitments and practices of asset managers, corporates, and financial institutions.

Some corporate CEOs have perhaps lowered their voices when it comes to ESG-related pronouncements, or even called for ESG terminology to go away. Nevertheless, ESG, climate change, and biodiversity are all clearly still top-of-mind in boardrooms, shareholder meetings, and private conversations of executives. This is evidenced further by their primacy in the World Economic Forum’s annual report of issues of concern for the business community.

Peering into 2023, an overarching question is whether the world of ESG and responsible business is shifting away from “win-win” such that businesses may have to choose between profitability and working to advance progress on major societal challenges.

The chapters that follow provide an oblique answer to this larger question. While abstract debates occupy headlines, the development of law and regulation when it comes to ESG continues at a rapid pace across the globe.

These legal and regulatory developments are the main subject of this book. Relevant laws and regulations will continue to shape business behavior – including strategy, governance and compliance, reporting and disclosure, external engagements and marketing – even after the trends of 2023 give way to those of 2024. The transition of “ESG” from the realm of voluntary frameworks and “soft law” to one of “hard law with teeth” is real and, ultimately, likely to be among the most enduring trends of recent years.

That transition is plotted out in detail in this publication, focused rigorously on legal and regulatory developments that businesses and those who advise them need to be aware of, as well as nonlegal drivers that also shape the business environment. We hope these chapters will add value as you navigate the pitfalls and opportunities that ESG generates for your organization.

We would like to extend our thanks to all the law firms that contributed so much to making this book what it is. Thank you also to the many Debevoise partners and associates who supported this project and contributed to its success. Our team at Debevoise includes lawyers with deep experience across the range of critical ESG issues, which proved essential to this project. In addition, without Gavin Collins and associates Toby Wenham Rogers, Miles Aho, Lisa Sheldrick, Maria Epishkina, Gavin Benson, and, in particular, Sophie Michalski, the pages you are about to peruse simply would not exist. Thank you, team!

We hope this is a useful resource to you and, as always, welcome your feedback on how we might make it even better.



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1. How is “ESG” in Argentina defined in a corporate/commercial context, and what are its major elements?

The term ESG is not defined in Argentinian legislation. However, there is legislation that regulates environmental, social and governance matters. The most recent rules in these areas are being interpreted by the legal community with a holistic approach.

Neither is the meaning of ESG agreed within corporate sectors. Typically, companies operating in the mining, extractive and energy industries emphasize environmental aspects, focusing on climate change mitigation and adaptation, energy transition and efficiency, pollution control, rational use of natural resources, sustainability, water and land use or waste reduce-reuse-recycle.

By contrast, companies operating in agrobusiness, food production and other labor-intensive industries focus on social aspects, considering the company’s impact on customers, employees, suppliers and the community in general. For instance: labor matters, diversity and gender equity, workplace safety, non-discrimination, inclusion, stakeholder engagement, public participation and community relations.

An emphasis on governance is shared across industries, but concentrated in listed companies and companies with high degrees of interaction with the government. Listed companies focus on corporate governance, shareholders’ rights, directors’ duties, compensation, board structure, reporting and auditing and investor relations. Companies that work with the government are concerned with corporate stewardship and accountability, integrity and compliance programs (anti-bribery, prevention of conflict of interest, anti-money laundering, anti-trust, protection of human rights) and risk and crisis management.

2. What, if any, are the major laws/regulations in Argentina specifically related to ESG?

ESG legislation in Argentina is mostly related to the issuance of sustainable financial instruments. The Securities and Exchange Commission of Argentina (CNV) has established a legal framework regarding sustainable issuances. This includes the Guidelines for the Issuance of Social, Green and Sustainable Marketable Securities, which follow internationally recognized standards such as the Green Bond Principles, the Social Bond Principles and the Sustainable Bond Guide developed by the International Capital Market Association (ICMA) and the Climate Bonds Standard. The CNV has also approved a new regime for sustainable collective investment products and a set of good practices to promote sustainable financing. The latter includes the following:

- socially responsible investment guidelines;
- guidelines for the issuance of social, green and sustainable bonds; and
- guidelines for external auditors.

3. What other laws/regulations in Argentina touch on ESG themes?

Additional laws, regulations and guidelines in Argentina that touch on ESG are:

- **Environmental legislation.** Argentina’s environmental legislation is relatively advanced and proactive in the protection of the environment. Much legislation

has been passed on the federal, provincial and municipal levels. The right to a healthy environment is included in the Federal Constitution.

Argentina applies the “polluter pays” principle and requires the approval of an environmental impact assessment before conducting certain risky activities. Moreover, legislation guarantees the right of access to environmental information, public participation in the environmental decision-making process and access to justice in environmental matters. Environmental insurance is required, and reporting duties are also established. Argentina has approved several human rights international treaties

- **Green procurement.** The Federal Government set a regime for sustainable procurement by public authorities, which requires consideration of sustainability when acquiring services and goods.
- **Energy transition.** The Federal Government has issued the guideline “Energy Transition Plan to 2030.” It aims to address climate change by implementing a structural change in the supply and use of energy systems. It tackles the decarbonization of the energy matrix and seeks to increase the production and distribution of affordable, reliable and clean energy, promoting energy efficiency and strengthening adaptation to climate change. The generation of electricity by renewable sources is promoted in Argentina.
- **Climate change.** Argentina has passed several climate change statutes and international treaties, e.g., the United Nations Framework Convention on Climate Change, the Kyoto Protocol, the Paris Agreement and, lately, a federal climate change law ((Law No. 27,520) which establishes minimum environmental protection standards to guarantee adequate actions, instruments and strategies for adaptation and mitigation to climate change).
- **Gender equality.** The Public Registry of the City of Buenos Aires has issued a resolution that requires gender parity on management bodies and statutory committees of legal entities based on the Federal Constitution and international human rights treaties (e.g., Convention on the Elimination of all Forms of Discrimination against Women).
- **Mandatory prior consultation to indigenous people.** Indigenous people’s rights are guaranteed in the Federal Constitution and several provincial laws. Argentina has approved the International Labor Organization Agreement No. 169 on “Indigenous and Tribal Peoples in Independent Countries,” which grants civil, politic, social and economic rights to indigenous and tribal peoples and proclaims respect for their culture and way of life. It establishes procedures to ensure the participation of indigenous peoples in the adoption of legislative or administrative measures that may affect them directly (i.e., free, prior and informed consultation process).
- **Prevention of forced labor.** Argentina has approved the International Labor Organization’s Agreements No. 29 and 105 on abolition of forced labor, 2014 Protocol and Recommendation No. 203.
- **Good corporate governance.** Following the Guidelines of the Corporate Governance Principles of the OECD. The CNV has requirements relating to independent directors.
- **Corporate compliance.** Legal persons are criminally liable for money laundering (Federal Law No. 25,246) and for corruption (Federal Law No.

27,401) offenses. The anti-money laundering regime establishes mandatory compliance programs for gatekeepers since 2000. By contrast, anti-bribery compliance programs were established in 2018 and, except for certain public contractors, are not mandatory (but are recommended to reduce sanctions through prevention and cooperation).

- **Human rights.** Argentina is a signatory member of all human rights treaties comprising the business & human rights legal framework. All such treaties have constitutional status, meaning the violation of the rights established in human rights treaties can be reviewed by the Federal Supreme Court.

4. What, if any, litigation or enforcement activity has Argentina seen related to ESG?

There has been no relevant litigation or enforcement activity regarding greenwashing yet. However, there are a number of high-profile cases related to environmental, social and governance matters:

- **Environmental.** Litigation of environmental issues is widely developed. Access to justice is guaranteed and, largely, free of charge for plaintiffs (mostly, NGOs). Legal standing is broad, and the Argentine judiciary tends to be proactive in environmental cases (judicial activism is popular when dealing with these cases). Both at the federal and provincial judiciary, claims are brought requesting remediation of contamination or the immediate halt of a damaging activity. Moreover, other environmental law principles create incentives for litigation (e.g., the principle of *in dubio pro natura*).
- **Anti-corruption.** Public and private enforcement has exponentially increased in the last few years, and has led to some of the corporate governance rules noted above in response to Question 2. The “Notebooks Case”, for the first time in Argentina, led to dozens of business leaders being indicted and requesting leniency in exchange for cooperation in a bribery scandal. Subsequently, auditors, business partners and lenders are much more cautious when dealing with corporates implicated in those criminal investigations.
- **Business and human rights.** Argentinian civil society has historically been very active in the enforcement of human rights abuses and violations. Particularly active is criminal enforcement of “business and human rights” violations, especially those related to labor exploitation, child labor and other labor abuses. Companies operating in extractive, textile and agricultural industries are most exposed to these claims.
- **Labor litigation.** Labor litigation is frequent and common. This is primarily because labour laws are considered public law, meaning that the rights granted to workers cannot be set aside by private contracts. Labor Courts consider employees to be in a weaker position in the employment relation. Consequently, measures that in any way limit or restrict the rights established by labor laws are deemed null and unenforceable. In addition, employees are exempted from paying court fees and taxes when initiating a labor claim. Further, Labor Courts follow the *in dubio pro operario* principle: any ambiguity in a contract is construed in favor of the employee. Recently, because of high inflation rates, unions have had an important role in negotiating salary increases.

- **Antitrust.** In a recent case, the Antitrust Commission extended the definition of “general economic interest” to include ESG considerations. Dow Química Argentina S.R.L. (DOW) intended to close a facility. In October 2021, the Antitrust Commission ordered a temporary injunction forbidding the alteration of DOW’s productive assets in relation to the facility, and started an investigation for abuse of a dominant position. “General economic interest” was interpreted broadly to include the contribution of the company to the well-being of the population and its economic interest (e.g., a healthier environment, better level of education, lower unemployment and better income distribution). Pursuant to the Antitrust Commission, the shut-down of the production may be deemed as an abuse of a dominant position, with clear negative effects in the community.

5. What are the major non-law/regulatory drivers of ESG trends and developments in Argentina?

Firstly, the general public and retail investors are not yet engaged in ESG as a holistic term. The general public demand companies act in a responsible manner, mainly focusing on large corporations. Public consensus on responsible business centers, mainly, on environmental, social, anticorruption and labor issues. At the same time, large corporations are those particularly engaged in ESG and pushing for a sustainable corporate agenda.

Further, there is no mainstream local shareholder activism. In Argentina, ESG is mostly market driven: the aim is mainly to fulfill consumers and stakeholders’ demands and to secure access to capital.

Secondly, various soft laws are currently being applied in Argentina. For instance, the 2030 Agenda for Sustainable Development, approved by the United Nations General Assembly in 2015, is currently being implemented in Argentina by the National Council for Social Policies. Moreover, the Anti-corruption Office (OA) regularly issues guidelines based on international standards to help companies establish or improve anti-bribery compliance programs. For example, a digital platform was recently launched to be used as a benchmark for integrity policies and procedures.

Further, the CNV and the Argentine Central Bank have approved a corporate governance code for companies subject to their supervision. This code is based on the “comply or explain” principle, and sets out various non-binding recommendations and guidelines. Only specific principles are binding, including independence requirements for members of a public company’s board of directors and syndics. The code provides for the following:

- promoting transparency in related-party transactions;
- setting rules for proper management and supervision; and
- supporting policies for effective risk management.

Lastly, with regards to national contact points, the OECD National Contact Point for Responsible Business Conduct has been appointed in Argentina (under the Ministry of Foreign Affairs and Worship) and has heard many cases during the last few years.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

Only some large local and multinational companies issue ESG annual reports, mainly in the form of sustainability reports (which are separate non-financial documents). Most of them follow Global Reporting Initiative rules, but they are not commonly audited by independent third-party reviewers.

The Federal Constitution sets out the obligation for the government to provide for environmental information and education. A citizen's right to free access to environmental information is guaranteed, particularly in relation to information held by public authorities. Companies must also disclose certain environmental information. Further, Argentina recently approved the Regional Agreement on Access to Information, Public Participation and Justice in Environmental Matters (Escazú Agreement). Its aim is to guarantee the full and effective implementation of the right of access to environmental information, public participation in the environmental decision-making process and access to justice.

7. Which sectors are most impacted by ESG in Argentina? How significant is ESG investment in Argentina?

The sectors that are most impacted by ESG are extractive industries, agribusiness, petrochemical and energy utilities. Those activities are, mainly, carried out by large companies (local and multinational), which have recently developed a strong ESG framework during. Public policies have been issued to specifically tackle these activities. For instance, environmental approvals for those activities usually require a public participation procedure and contain ESG requirements (e.g., hire local employees, buy from local suppliers, contribute to infrastructure public development funds, work on stakeholder engagement, develop social communication plans).

8. What are the trends in Argentina regarding ESG governance?

Companies are conscious that ESG measures should be integrated and proactive. ESG governance reflects both integrated structures (or several thematic structures reporting to a single Chief Risk Officer) and mandates oriented to prevent risks, not to react to incidents and complaints.

Governance structures do not follow any particular "local" trend, but follow usual patterns of corporate internal organization. Subsidiaries of multinational companies tend to replicate structures decided in their home countries, with direct reporting lines to either regional or global sustainability committees. The identifiable trend, as in many other countries, is to reorganize all compliance structures (environmental, anti-bribery, anti-money laundering, fraud, antitrust, etc.) under the oversight of a single officer (e.g., Chief Risk Officer).

While this is the case in most financial and listed companies, there is still a wide spectrum of large local business groups and small and medium enterprises where the ESG governance structures, when they exist, tend to be incipient and exploratory. For these companies, the ESG agenda could be spread among sustainability officers and/or allocated in other existing areas (e.g., communications, public/external/corporate affairs).

9. To what extent are ESG ratings or ESG benchmarks relied upon in Argentina?

There is no unique or established ESG benchmark in Argentina yet. Regarding financing, the CNV follows worldwide accepted tools to provide assurance to investors on the ESG credentials of the financial instruments used, among which is external reviews. These are suggested to issuers to reinforce the credibility of the label of the security used to finance green and/or social projects. The most common forms of external reviews are:

- a second opinion from an independent institution;
- verification by an independent third party;
- certification of the issuer's green security *vis-a-vis* an internationally recognized and publicly available standard; and
- rating/scoring.

10. What is the role of the private markets versus public markets in driving ESG developments in Argentina?

A great number of large national and multinational companies in Argentina have applied ESG policies. It is mainly market driven: policies have been adopted due to stakeholders and finance demands. Very few SMEs in Argentina have integrated ESG issues in their business strategies; the current local economic and financial situation is the focus.

Private markets are also driving the "G" agenda. Many investigations and remediation processes are requested by auditors, business partners or financial institutions. The hierarchization of compliance departments is also market driven. Compliance is evolving from bureaucratic and low-rank structures towards higher-ranked and prestige positions within corporates. As a result, Chief Risk Officers are now frequently consulted by board members when taking strategic and long-term decisions, and are entrusted to assess risks over new products, businesses lines or new markets, as well as to engage with senior regulators in policy discussions affecting the business.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

The major challenges for companies facing ESG obligations are:

- to integrate compliance areas touching ESG topics (environmental, social, labor, anti-corruption, anti-money laundering, antitrust) under a single compliance structure;
- to find a cost-effective way to ensure compliance with each of these subject matters, following benchmark guidelines and being externally audited for quality assurance; and
- to comply with disclosure requirements to assure the public that the funds raised in an issuance are used for the purposes for which they have been invested – validation by independent external reviewer is becoming best practice.

12. What information sources are most relevant for ESG considerations in Argentina?

There are various high-profile NGOs that can be classified based on scope and line of business. Some of them focus on environmental issues, both local and global, while others focus on social or governance affairs (transparency, democratic institutions' quality and so on). There is no ESG-only focused NGO or think tank yet, nor any private measurement frameworks or ESG-only benchmarks.

13. Has Argentina developed a Taxonomy related to ESG?

No.

14. What does the future hold for ESG in Argentina?

Notwithstanding current economic and financial turmoil, Argentina continues to adopt ESG policies and, overall, setting public policies to achieve sustainable development. Certainly, there are many areas in which long-term decision-making is postponed for tackling urgent concerns. However, the potential role of Argentina in global food and energy security seems to be driving several specific bills that will make ESG principles more effective in agribusiness, energy transition and mining (lithium and copper, mainly). ESG policies would play a pivotal role in the development of these areas, as well as its financing.

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1. How is “ESG” in The Bahamas defined in a corporate/commercial context, and what are its major elements?

In The Bahamas, particular emphasis is placed on “Environmental” and “Governance.” The Environmental emphasis is fairly new and can be attributed to global attitudes shifting towards protecting the environment. The Bahamas has considered its impact on the global environment with the introduction of new environment-focused legislation (see below, Questions 2 and 3). Emphasis on Governance is something that has always been present. As it constantly evolves, it can be better traced. This emphasis is evident through our legislation, which continues to be updated, and the existence of various regulatory entities.

Governing regulatory bodies include:

- Central Bank/Inspector of Banks and Trust Companies, responsible for, *inter alia*, monetary stability, encouraging economic development, safeguarding a stable, adequate financial system and ensuring proper supervisory oversight for supervised financial institutions.
- Securities Commission of The Bahamas/Inspector of Financial and Corporate Service Providers, responsible for, *inter alia*, regulating and overseeing investment funds, securities and the capital markets and ensuring that all persons operate in accordance with the Financial and Corporate Service Providers Act, 2000, which provides for the licensing and regulation of financial and corporate service providers.
- Compliance Commission of The Bahamas, responsible for, *inter alia*, maintaining a general review of financial institutions (inclusive of Designated Non-Financial Business and Professions (DNFBPs)) in relation to the conduct of financial transactions and to ensure compliance with the provisions of the Financial Transactions Reporting Act, 2018 (FTRA), and that financial institutions and DNFBPs meet best international standards and practices, consistent with the provisions of Bahamian Anti-Money Laundering (AML), Countering the Financing of Terrorism (CFT) and Countering/Proliferation Financing (CPF) legislation.
- Insurance Commission of The Bahamas, responsible for, *inter alia*, surveillance over the insurance market as well as promoting and encouraging sound and prudent insurance management and business practices.
- Utilities Regulation and Competition Authority (URCA), responsible for, *inter alia*, the Electronic Communications Sector (ECS) and the Electricity Sector (ES). In the ECS, URCA issues licences and exemptions, manages state assets and applies competition law rules. As regulator of the ES, URCA is responsible for all persons and/or entities that generate, transmit, distribute or supply electricity to, from or within The Bahamas.
- Bahamas Maritime Authority, which aims to promote, facilitate and encourage the development of ship registration and maritime administration, to regulate control and administer all matters related to merchant shipping, to participate in international organizations and other meetings dealing with maritime-related matters, to develop the maritime industry of The Bahamas, to expand and create maritime employment opportunities for Bahamians and to advise Government on any matter relating to merchant shipping, marine pollution prevention and control.

2. What, if any, are the major laws/regulations in The Bahamas specifically related to ESG?

Major laws relative to ESG include the Environmental Planning and Protection Act, 2019 (EPPA) whose objective, *inter alia*, is to “protect the environment of The Bahamas while providing for development in a way that maintains ecological integrity and the social and economic welfare of local communities.” The EPPA makes it mandatory for an individual or entity to obtain a government-issued Certificate of Environmental Clearance before they can start working on a building project where there will be man-made change to the environment. This is to better regulate construction and its effects on the environment in the jurisdiction.

More recently, the Climate Change and Carbon Markets Initiatives Bill, 2022 and the Carbon Credit Trading Bill, 2022 have been tabled. One of their biggest objectives, if passed, would be to regulate carbon trading in the jurisdiction.

The Central Bank of The Bahamas Act and the Banks and Trust Companies Regulation Act of 2000, which dictate the governance of the Central Bank, one of the biggest regulatory entities in this jurisdiction, received an overhaul in 2020. They were amended to align with the best international practices and to maintain a durable financial system.

The FTRA requires all institutions, which in their day-to-day function administer and manage funds on behalf of others, to perform due diligence measures and keep records of risk assessments when conducting business with a new client. The FTRA also requires the reporting of anything that warrants suspicion upon the performance of risk assessments and due diligence measures, along with any other suspicious transactions.

The Commercial Entities (Substance Requirements) Act, 2018 requires certain relevant entities in this jurisdiction to submit annual economic substance reports. In certain circumstances, those reports must detail gross income, amount of expenditure, number of employees, etc. to ensure that these entities are engaging in legitimate economic activity and have economic substance in The Bahamas.

3. What other laws/regulations in The Bahamas touch on ESG themes?

The Prevention of Bribery Act of 1976 (amended in 2014) and the FTRA place attention on anti-corruption and anti-money laundering, respectively. While this legislation may not be specifically linked to ESG, the themes it touches upon fall within the “G” of ESG. Similarly, the Employment Act of 2001 (amended in 2017) *inter alia* protects employees and job applicants from discrimination “[...] on the basis of race, creed, sex, marital status, political opinion, age or HIV/ Aids,” which falls within the “S” or Social theme of ESG.

There is no relationship between antitrust laws and sustainability issues. While The Bahamas has no general antitrust laws, there are three antitrust statutes that are industry-specific. The Communications Act and the Utilities Regulation and Competition Authority Act (both of 2009) together with the Electricity Act of 2015 regulate the electronic communications industry and electric industry, respectively, but do not make mention of sustainability issues.

4. What, if any, litigation or enforcement activity has The Bahamas seen related to ESG?

The Central Bank of The Bahamas is the ultimate enforcer against licensees and regulates all banks and trust companies operating within the jurisdiction. The Central Bank's website provides that, "pursuant to [t]he Banks and Trust Companies Regulation Act, [2020] and Central Bank Act, [2020] the Central Bank of The Bahamas is responsible for the licensing, regulation and supervision of banks and trust companies operating in and from within The Bahamas. As such, all licensees are expected to adhere to the Central Bank's licensing and prudential requirements and ongoing supervisory programmes, including periodic onsite inspections, and required regulatory reporting." (See www.centralbankbahamas.com.)

Similarly, the regulatory bodies previously mentioned, i.e., the Securities Commission, Compliance Commission, Insurance Commission, etc., would be the entities responsible for the enforcement of any irregularity or breach of regulation in their specific industry.

Additionally, the Financial Intelligence Unit, an agency established by the Financial Intelligence Unit Act of 2000, is an agency whose responsibility, as outlined by the Act, is to receive, analyse, obtain and disseminate information received in suspicious transaction reports that may relate to proceeds of crime relevant to the Proceeds of Crime Act, 2018 and/or the Anti-Terrorism Act, 2018. This agency works actively with the Royal Bahamas Police Force to investigate potential threats and to enforce any breach of the aforementioned legislation.

5. What are the major non-law/regulatory drivers of ESG trends and developments in The Bahamas?

Soft non-binding laws

The Bahamas generally supports and promotes soft non-binding laws. Since becoming a member of the International Labour Organization (ILO) in 1976, The Bahamas has ratified, *inter alia*, the organization's convention on forced labour. Subsequently, in 2011, The Bahamas adopted the UN Guiding Principles of Business and Human Rights.

In 2014, a 25-year National Development Plan was developed, with the government claiming to have ensured that the UN's 2030 Agenda and Sustainable Development Goals were considered during the plan's development.

In response to the Organization for Economic Co-Operation and Development (OECD) Guidelines for Multinational Enterprises, The Bahamas passed the Multinational Entities Financial Reporting Act of 2018 (the MNE Act). The MNE Act was inspired by the Base Erosion and Profit Shifting (BEPS) initiative of the OECD. BEPS refers to strategies used by entities to avoid the payment of taxes that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations (www.oecd.org/tax/beps). The MNE Act requires entities with revenues of BSD 850 million or more to annually file a country-by-country report with the Minister of Finance.

Stakeholders

In addition to the promotion of soft law, the government is also concerned with ESG in general. The government is motivated by operating in the best interest of the people and Bahamian resources. Companies are motivated by the desire to make profits and satisfy consumers. In a jurisdiction where consumers are not primarily interested in ESG-related issues, companies do not have to concern themselves with the promotion of ESG trends.

The general public

The general public's concern for ESG-related matters is difficult to gauge due to a lack of data. Similarly, local companies are not particularly concerned with ESG. However, according to the Attorney General, foreign investors have taken an interest in ESG-investing in The Bahamas, specifically by purchasing blue carbon credits from the Bahamian government.

The public's interest in ESG and investment attitudes is again difficult to gauge due to a lack of data. However, when looking at the findings discussed below, it can be assumed that the average retail investor is not greatly concerned with ESG-related matters.

Institutional investors

The Corporate Governance Survey 2022 of PwC Bahamas (the Survey) states that 56% of Bahamian board directors admitted that their board had no defined process of ESG oversight. Similarly, the Survey states that 50% of board directors indicated that they did not directly engage with shareholders. As it appears that shareholder opinions regarding ESG are not of high value to Bahamian boards, it cannot be said how much of a role, if any, shareholder activism plays in promoting ESG considerations. The Survey notes that the lack of contact with shareholders is uncommon in other jurisdictions, but ultimately concludes that ESG is not heavily considered in the governance of most boards in The Bahamas. The survey goes on to state that only 13% of board directors believed that ESG reports impacted shareholder investment decisions.

Companies

It has already been established that local companies are not concerned with a sustainable corporate agenda. Over 40% of local board directors admitted to not understanding material ESG risks nor ESG messaging.

Foreign companies looking to promote a sustainable corporate agenda see The Bahamas as an opportunity to appear sustainable without actually reducing their carbon footprints. The Bahamas is home to many mangrove ecosystems and is in possession of blue carbon credits that the government does not need due to the country being net negative in carbon emissions. Companies who are either unable or unwilling to reduce their carbon footprints have offered to purchase these blue carbon credits from the Bahamian government so that they are able to meet carbon emission requirements without having to actually reduce their carbon emissions.

The government

The government is proactive in the promotion and regulation of responsible business practices to a certain extent. The aforementioned Communications Act and Utilities Regulation and Competition Authority Act both forbid anti-competitive agreements, regulate mergers that can suppress competition and prohibit companies from exploiting their dominance in the industry. Furthermore, the Utilities Regulation and Competition Authority Act established an authority of the same name, which ensures that all telecommunication and utility companies in The Bahamas are operating within the law.

Moreover, the Climate Change and Carbon Markets Initiatives Bill, 2022 and the Carbon Credit Trading Bill, 2022 are currently being pushed and, if passed, would regulate all carbon trade in the country and would require reports of carbon emissions. It is evident that some effort is being made in addressing ESG-related issues.

Greenwashing is a concern and is explicitly referenced by the Office of the Prime Minister. "A carbon credits system would help the planet...the project will be based on science and will not amount to 'greenwashing' or providing an escape clause for people to continue emitting greenhouse gases" (see www.tribune242.com/news/2022/apr/22/carbon-credit-buyers-have-approached-government). It is this fear of greenwashing that is motivating the government to put legislation in place that will regulate carbon trading before selling carbon credits to the first bidder.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

The EPPA requires individuals and companies to disclose instances of spills or other accidental release of pollutants into the environment. Similarly, the Commercial Entities (Substance Requirements) Act, 2018 requires entities to disclose information regarding profit and expenditure and board directors to prove the legality of the entities' economic presence in the jurisdiction. However, in neither case is a process prescribed to measure the output of what is being reported.

Reporting

Currently, as ESG reporting is not mandatory in this jurisdiction, there are no set regulations for when reports are to be updated. For the companies that do participate in ESG reports, it can be assumed that the findings are reported to their shareholders in some kind of periodic communication.

The only known firm that conducts ESG reporting in this jurisdiction (Deloitte) has expressed its support of the International Sustainability Standards Board (ISSB). In their 2021 Financial Brief, Deloitte said that "ISSB will take account of and build on the substantial work done by many leading global organisations in the area of sustainability and the underlying environmental, social and governance (ESG) factors over recent years."

7. Which sectors are most impacted by ESG in The Bahamas? How significant is ESG investment in The Bahamas?

ESG is still too new in this jurisdiction to determine what sectors are most impacted by ESG, as a few industry leaders are just now starting to consider ESG collectively. While Environmental and Governance have been the focus for legislators, we do know that the consideration for ESG is growing.

The parent company of one of the largest electronic communication companies in The Bahamas is Liberty Latin America (LLA). In July 2022, LLA released its second annual ESG report “outlining the company’s commitment to environmental, social, and governance (‘ESG’) practices across its operations in Latin America and the Caribbean” (see [ewnews.com/btcs-parent-company-lla-releases-2021-esg-report](https://www.ewnews.com/btcs-parent-company-lla-releases-2021-esg-report)). In the news article, LLA’s CEO, Balan Nai, stated that the 2021 ESG report shows that the company is committed to “responsible and sustainable practices across our operations in Latin America and the Caribbean.”

8. What are the trends in The Bahamas regarding ESG governance?

The title of “Chief of Sustainability” is not becoming a common trend, though comparable titles are seen across various fields in the jurisdiction. The University of The Bahamas has a Sustainability Committee headed by a Sustainability Coordinator, Bahamar (a major hotel brand) has a Sustainable Director and the government has recently appointed a new Director of Environmental Planning and Development. Similarly, specialized ESG committees are now being created by executive boards.

Beyond this, there appears to be a growing interest in the social aspect of ESG on Bahamian boards, with over 80% of respondents to the Survey stating that they had invested, or plan to invest, in up-skilling of their employees. Further, over 30% of respondents answered that they believed that there should be more conversations about diversity and inclusion at the board level. Moreover, 50% of respondents believe that their companies should have a wider social purpose, nearly 40% believe that their companies should be doing more to promote diversity in the workplace and 69% have stated that ESG-reporting and disclosure should be a priority for management. While these findings display at the very least some interest in ESG, they are mostly just beliefs that some changes should be made and do little to prove any actual change.

The most notable trend would be legislation relating to ESG. Most of the legislation referenced in Question 2 has either come into effect or been amended within the last four years.

9. To what extent are ESG ratings or ESG benchmarks relied upon in The Bahamas?

ESG rating agencies

Deloitte provides ESG rating services, but it is not known how often those are utilized. It can be assumed that ESG ratings are not often used, given the lack of attention to ESG by board directors and the opinion of directors that investors do not care much about ESG ratings.

10. What is the role of the private markets versus public markets in driving ESG developments in The Bahamas?

Private companies

The Survey states that ESG is not currently prioritized by many boards when forming business strategies, citing a lack of awareness as a contributing factor. Despite this, issues relating to ESG, such as income inequality and human rights, are heavily considered when developing strategy, with both being in the top percentile of issues considered. Climate change and social movements are also considered but on a smaller scale.

Public companies

Pursuant to the Survey, over 40% of Bahamian board directors admitted to not understanding the material risks of ESG. Further, 38% admitted that ESG issues were not linked to their company's strategy.

Government-owned organizations

Government-owned organizations have given more attention to ESG considerations in recent years, although it would be inaccurate to refer to ESG considerations as "key" to these organizations.

ESG agenda

The ESG agenda is mainly being pushed by international organizations of which The Bahamas is a part, namely the UN and ILO. The local government has become more concerned with matters pertaining to ESG, but as mentioned from the beginning, the focus is on Environmental and Governance, and not much emphasis is being placed on the Social aspect.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

The main barrier to effectiveness is a lack of action being taken. Throughout this chapter, there have been several references to the Survey, which states that a large portion of respondents believe that ESG should become more of a priority, and that more should be done to push an ESG agenda both inside and outside of the workplace. Yet only 25% of Bahamian board directors report that ESG issues are regularly a part of their agendas. This small percentage reflects how little action is being taken by companies to prioritize the ideas that they claim should be prioritized. Moreover, only 6% of respondents believe that their boards understand ESG risks well. Such a small figure is concerning when contrasted with the number of respondents who claim to want to make ESG a priority. This reveals another barrier to effectiveness, namely a general lack of knowledge surrounding ESG in The Bahamas. The fact that participation in ESG reporting is not mandatory in this jurisdiction contributes to the lack of priority and to unawareness that inhibits effectiveness. As only 13% of respondents felt that ESG reporting was too expensive, high costs are not much of a barrier. There is no available data to suggest that public opinion is a factor in ESG's lack of effectiveness in this jurisdiction.

12. What information sources are most relevant for ESG considerations in The Bahamas?

The most relevant sources for ESG considerations would be reports required under different legislation and the occasional corporate survey. However, given that there is already a focus on “Environmental” and “Governmental,” it may be prudent to consider the mission of certain NGOs, particularly in this jurisdiction, where there is less legislative development with regards to “Social.”

The Organization for Responsible Governance (ORG) is an NGO that has three main focuses: Accountable Governance; Education Reform; and Economic Development. ORG “serves as a bridge uniting stakeholders from a diverse cross-section of society in pursuit of a common vision: a thriving Bahamas where accountable and transparent governance allows each individual, business and group a say in decisions that affect our future and equal access to opportunity” (see www.orgbahamas.com). ORG works with like-minded partners to fuel civil society groups around issues of mutual interest, fosters collective action and encourages capacity-building and development in advocacy groups.

The Nassau Institute is a think tank that should also be approached as an information source for ESG consideration. The Nassau Institute’s “mission is to formulate and promote public policies for The Bahamas based on the principles of limited government, individual freedom, and the rule of law” (see www.nassauinstitute.org/about-the-nassau-institute). Both ORG and The Nassau Institute can provide valuable insight to social factors that need to be addressed in ESG considerations.

13. Has The Bahamas developed a Taxonomy related to ESG?

There is no Taxonomy related to ESG in this jurisdiction.

14. What does the future hold for ESG in The Bahamas?

With the increased awareness of ESG in The Bahamas and the legislative initiatives taken by the government thus far, this jurisdiction will most likely see various developments over the next few months and years to come.

In the short term, we will probably see an increase of ESG role designations in entities and organizations and more education forums for the public at large and private entities.

In the medium term, we will most likely see more ESG-focused legislation considered by the government, particularly on the “Social” aspect, which is lacking, and perhaps there will be more of a push for more legislation for this area. We should also expect an increase in surveys to determine the public and commercial view of ESG.

In the long term, The Bahamas may pass more ESG-friendly legislation that is conducive to development and business opportunities. We will most likely see an increase in rating exercises and surveys and an influx of investors and developers canvassing or entering the jurisdiction for opportunities. Likewise, this jurisdiction saw huge developments and the migration of key industry players in the digital asset space when modern and advanced legislation was created. The Bahamas recently passed the Digital Assets and Registered Exchanges Act, 2020 (amended in 2022) (DARE Act). This Act, *inter alia*, regulates the issuance, sale and trade of digital assets in or from within the jurisdictions. The DARE Act is innovative and was one of the first of its kind in the region. Since its commencement, we have seen an immense interest by entities wanting to do business in The Bahamas.

The Bahamas has witnessed and proven that where there is legislation to facilitate the ease of doing business, industry opportunities and development will follow. The Bahamas is keen to introduce legislation that is well positioned with the highest international practices and standards. ESG efforts are no exception, and we already see the shift happening.

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Vanessa is a partner of McKinney Bancroft & Hughes, whose areas of expertise include real estate transactions and development, corporate transactions, financial services and private client wealth management.

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Vanessa is passionate and driven and believes in upholding the integrity of the profession. She possesses excellent problem-solving skills, and her clients admire the way in which she always makes herself accessible to them.

Outside of the law, Vanessa is passionate about cooking and baking plant-based cuisine, and she also enjoys community service, laughing with friends and spending time with her family.

BRAZIL

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1. How is “ESG” in Brazil defined in a corporate/commercial context, and what are its major elements?

ESG in Brazil is a combination of practices which aim to make the corporate environment more inclusive, ethical and sustainable. The foundation of modern “ESG” in Brazil is based on the UN Global Compact 2004 publication “Who Cares Wins,” and purports to align profit, purpose, sustainability, ethics and transparency. ESG has been in the spotlight in Brazil since the corruption scandals implicating several high-profile companies in different industries, along with the pandemic, the war in Ukraine and constant concerns over climate change.

ESG regulations in Brazil largely follow global standards in terms of adopting the soft law approach of ‘comply or explain’. The ESG market has consistently gained traction through the adoption of ESG metrics by pension funds in their investment decisions (which represent the core of Brazilian institutional investors with over BRL 1 trillion – circa USD 200 billion – of assets under management), the formation of funds focused on impact investing and the widespread implementation of ESG policies by companies in need of funding from venture capitalists, private equity firms or through the capital markets.

Brazilian legislation also plays a key role in such a rapid and smooth adoption of ESG practices. Even prior to the rise of global ESG trends, Brazil had many ESG-related regulations across each of the three core elements:

- **Environmental.** The Brazilian Constitution, promulgated in 1988, established (among other topics) the need to promote social justice and protect the environment as a fundamental principle. The same applies to the National Environment Policy Law No. 6,938/1981, which promotes and enforces sustainable economic development.
- **Social.** The Consolidated Labor Laws (Decree-Law No. 5,452/1943), among other matters, forbids discrimination in the workplace.
- **Governance.** The Brazilian Corporations Law (Law No. 6,404/1976) was significantly ahead of its time and represented a fundamental step towards future ESG policies. It has brought in at several critical concepts.

One is a definition of stakeholders – controlling shareholders and managers must ensure that a company observes not only the interests of controllers, but also of minority shareholders, employees, customers, suppliers and the community in which the company is based. Second, is that such law also demands that both controllers and managers ensure the company follows its social function in the developing of its activities.

Moreover, since the early 2000s, the Brazilian stock exchange (B3) has developed a sophisticated set of voluntary regulations applicable to listed companies who decide to list their shares in different corporate governance segments. This includes the *Novo Mercado* regulations, which require companies to adopt more robust governance and reporting practices.

Finally, since 2013, several corruption scandals have emerged in Brazil, particularly the *Car Wash* operation. This operation started off as an investigation into money laundering before expanding to uncover a vast and intricate web of political and corporate racketeering. *Car Wash* has led to the adoption of several local laws and regulations enforcing international standards of anti-bribery and corruption and anti-money laundering, namely the Clean Company Act No. 12,846/2013.

2. What, if any, are the major laws/regulations in Brazil specifically related to ESG?

The following are the major laws/regulations specifically related to ESG:

- Resolution 59/2021 (effective as of the beginning of 2023), issued by the Securities and Exchange Commission of Brazil (CVM), operates similarly to Directive 2014/95/EU, and requires listed companies to provide information on ESG practices and indicators in a reference form (equivalent to the U.S. 20-F) under a “comply or explain” basis. This form is required on an (at least) annual basis, and is subject to investigation and administrative penalties in case of misrepresentation. This resolution lists many ESG-related topics requiring the company to explain their practices, including: (i) where they publish their ESG matters; (ii) if such publications are audited by any independent advisor; (iii) the adoption of any (and which) ESG key performance indicators; (iv) greenhouse gas emissions; (v) business opportunities related to ESG; (vi) ESG risk factors potentially affecting decisions by the company investors; (vii) the role of managing bodies in ESG matters; (viii) the existence of internal channels permitting the flow of ESG information/complaints; and (ix) ESG elements affecting management compensation.
- Resolution 139 and Normative Instruction 153, issued by Brazil’s Central Bank, requires the (at least) annual disclosure of a Social, Environmental and Climate Risks and Opportunities Report.
- Resolution 4.327 provides the guidelines that must be observed in the establishment and implementation of the Social and Environmental Responsibility Policy by financial institutions.
- Resolution 4.945, issued by the National Monetary Council, which amended the Social and Environmental Responsibility Policy to the Social, Environmental and Climate Responsibility Policy.
- The Brazilian Stock Exchange (B3) listing segment self-regulations (Bovespa Mais, Nível 1, Nível 2 and Novo Mercado) have, since the early 2000s (and through constant updates), been incrementally increased governance standards. These include, among other matters (and variances depending on the segment adopted), quarterly and more detailed financial reporting, audit committees, the presence of independent directors, one share one vote, enhanced rights to minority shareholders such as full tag along rights and so on.
- Decree 11,075/2022, created the Regulated Brazilian Carbon Market, Law 12,305/2010, implemented the National Policy on Solid Waste.
- Law 14,119/2021 regulates the National Policy for Environmental Services Payment, a financial incentive to promote environmentally-friendly services.

3. What other laws/regulations in Brazil touch on ESG themes?

The Brazilian legal system has a strong tradition in environmental and labor regulations. Under Law 9,605/1998, companies and individuals may be criminally liable for damages caused to the environment. Other

environmental laws establish policies and standards for activities developed in environmentally sensitive areas, hazardous waste disposal, water waste and effluent standards, use of chemicals, environmental licensing and multiple other areas.

Brazilian environmental law is moving towards incentive policies rather than prohibitive directives, rewarding companies that follow certain principles – for example, Decree 10,828/2021 introduced the “Green Credit Certificate,” a credit instrument awarded to finance reforestation activities and the maintenance of native vegetation on rural properties.

Social aspects of ESG are often covered by labor regulations, which are strictly enforced. Brazil is a party to most international treaties on human rights and treaties under the Organization of American States and the International Labor Organization. The substantive human rights are mainly provided for in these treaties and in Brazilian Federal Constitution.

Additionally, Federal Decree No. 9,571/2018 internalizes the UN Guiding Principles on Business and Human Rights, establishing further guidelines on human rights that may be voluntarily implemented by companies in Brazil.

The CVM and the Brazilian Corporations Law establish multiple governance minimum principles that must be followed by public companies, regarding minority shareholders protection and the role of shareholders and management. The Brazilian stock exchange (B3) also requires some minimum governance standards for companies listed therein.

4. What, if any, litigation or enforcement activity has Brazil seen related to ESG?

Brazil has broad environmental-related restrictions and, as such, the country has seen notable cases of climate-related litigation. In 2022, the Superior Court of Brazil (STJ) has been ruling over a so-called “Green Package,” a number of seven proceedings related to the protection of the Amazon Forest, and addressing climate emergencies. So far, the court has decided in favor of the environment.

Brazil has seen enforcement of anti-greenwashing legislation through the lens of consumer protection. In 2013, the National Council for Advertising Self-Regulation ruled against companies that carried misleading advertising practices about the sustainability of its products (*Group of Consumers v. Usina São Francisco, Representation 087/13* and *Conar v. Organique Brasil, Representation 046/13*).

Brazil has a long tradition on the enforcement of labor laws, such as the Ministry of Labor and Social Security’s “Dirty List” of Slave Labor, which periodically publicizes companies that have been found to employ slave labor. Additionally, spontaneous investigations may be conducted by the Public Ministry of Labor to investigate any unlawful procedures in companies, often resulting in labor public actions and penalties.

Finally, non-compliances with mandatory governance and disclosure standards by public companies and financial institutions are overseen by the CVM and Central Bank, which can impose administrative penalties, varying from warnings and fines to suspension or disqualification.

5. What are the major non-law/regulatory drivers of ESG trends and developments in Brazil?

Soft non-binding laws

Brazil promotes ESG through multiple soft law instruments. The annual CVM directive release reinforces governance practices to be followed by companies. Since 2017, Brazilian Institute of Corporate Governance (IBGC) has published the Brazilian Corporate Governance Code which has been adopted by the CVM, also under the “complain or explain” approach. B3 is also proposing that public companies abide by minimum diversity standards. Finally, many companies utilize the UN Sustainable Development Goals as the basis for internal policies and initiatives.

Stakeholders

Stakeholders have been key in developing ESG in Brazil. As the appetite for sustainable investment has grown nationally and abroad, multiple associations, institutional investors and the retail market has demanded further development of ESG standards in the country, often copying international development.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

Reporting

Virtually all specific ESG regulations highlighted in response to Question 2 are primarily related to corporate disclosure. Other, older, non-specific ESG laws and regulations are not related to corporate disclosure but rather compliance with standards contained therein, and are subject to investigation and penalties.

Considering that all such ESG-specific regulations are relatively new, most companies have not yet been able to produce comparative reports or internal ESG data, and many of the reports disclosed are limited to describing generic ESG matters without reference to a recognized taxonomy framework.

7. Which sectors are most impacted by ESG in Brazil? How significant is ESG investment in Brazil?

ESG implementation has been a trend in all areas of the Brazilian economy, but some sectors have been impacted more than others.

Agribusiness

The agricultural sector in Brazil has developed with a focus on efficiency, but has always been highly regulated and supervised by governmental authorities aiming to curb environmental damage. The Regulated Brazilian Carbon Market, the National Policy for Environmental Services Payment and the Green Credit Certificate set out incentive policies that heavily influence the producers to adopt ESG development.

Energy industry

Brazil has always been an international example of clean energy generation. In 2021, the Ministry of Mines and Energy created the “Fuel of the Future” committee

(Resolution CNPE No.07/2021), aiming to develop biomass, biodiesel and other sustainable fuel alternatives.

Banks

The Brazilian Central Bank has been at the frontline of the establishment of an ESG financial framework in Brazil. Banks have to comply with multiple directives relating to ESG financial disclosure and management, as well as accounting for climate, social and environmental risks in their business.

Private equity and venture capital

Private Equity and (mostly) Venture Capitalists have rapidly understood the importance of offering specific ESG-related products to their investors, and have been playing a key role in both forming specific impact investing funds and incentivizing companies to adopt strong ESG practices (sometimes more comprehensively than specified under existing laws and regulations) in order to receive funding.

Pension funds

The National Superintendence for Pension Funds (Previc) oversees Brazilian closed pension funds, which has a significant role in the development of the equity capital markets in Brazil. A recent study, published in September 2021 (and reported in the reputable newspaper Folha de São Paulo), found that 56% of Brazilian pension funds adopt ESG metrics in their investment decisions. Of those, 40% integrate ESG factors systematically, and 81% use those factors to help them manage the investment risks.

This report also incentivized the adoption of more standardized reporting mechanisms by companies to facilitate the pension funds' task of finding and monitoring ESG investment opportunities. The publication of the report was prior to the passing of CVM's Resolution 59, which also purports to resolve the current lack of disclosure of ESG metrics.

8. What are the trends in Brazil regarding ESG governance?

ESG matters can be addressed by Boards of Directors, particularly in companies that have not been able to build a more detailed and specialized corporate structure. Boards may take into consideration information and advice provided by technical advisory committees, such as sustainability or diversity committees, where existent. Increasingly, variable compensation (including bonuses) has been linked to executives meeting ESG goals. The adoption of governance and corporate policies enforcing ESG standards are growing, as well as more robust due diligence checks and processes for mapping internal and external ESG risks and impacts.

Another initiative is the creation of specific committees to work on social-related issues, such as gender-based disparities. Some companies establish governance metrics and goals, committing to, for example, a certain percentage of female participation in high management and on the Board. As such, as new ESG metrics become more standardized, it is expected that specific ESG committees, either at Board or executive level, will become the *de facto* norm in Brazil.

9. To what extent are ESG ratings or ESG benchmarks relied upon in Brazil?

ESG rating agencies

The Brazilian market follows ESG rating agencies used worldwide, such as S&P, Moody's and Fitch. As such, rating agencies often follow parameters established by foreign countries; they may cause distortions and fail to appreciate internal or specific concerns, but those concerns can be explained by companies in their disclosures.

ESG benchmarks

ESG benchmarks have been growing in Brazil, with multiple ratings issued in the last couple of years. These include ISE-B3, MSCI's ESG Rating and S&P/B3 Brasil ESG. Considering the lack of ESG standardization and the multiple indicatives adopted (and often adapted from foreign systems, as above), it is expected that the ESG ratings and benchmarks will increase in effectiveness once ESG implementation reaches the next step of development in Brazil, particularly from 2023 when CVM's new Resolution 59 will become effective.

10. What is the role of the private markets versus public markets in driving ESG developments in Brazil?

The ESG agenda is pushed mainly by private investors, by stakeholders and by international bodies. However, regulators have been increasingly focusing on ESG standards, as outlined in the responses to Questions 2 and 3.

Reducing negative environmental impact is a common initiative by companies: focusing on the minimization and recycling of waste, water conservation and energy conservation programs. Increasingly, companies set goals to become carbon-neutral or carbon-efficient. Acquiring carbon credits and issuing ESG bonds and green bonds is also a practice on the rise, following government incentives to do so (see the response to Question 3).

From 2023, when the CVM's Resolution 59 takes effect, we will start to see more accurately the public market's role in ESG matters. In Brazil, public companies generally have more sophisticated internal policies and resources to implement changes, such as those required by ESG standards. As such, it will be interesting to see how the public markets react to companies more focused on "explaining" their lack of ESG practices and to those actually able to evidence their "compliance" to ESG standards. Hopefully, the latter will experience better results when subject to similar industry and market conditions.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

The next chapter for ESG in Brazil is developing an ESG taxonomy standard to enable better comparability of the ESG disclosures issued by companies (see the response to Question 13). We expect CVM's Resolution 59 will solve part of that problem with respect to listed companies. However, the private market still lacks standardized data collection and access. Standardization will allow for a more comprehensive decision-making process regarding investing, incentivizing, monitoring and supervising ESG integration.

12. What information sources are most relevant for ESG considerations in Brazil?

The World Resources Institute (WRI) and the World Wide Fund for Nature (WWF) are NGOs with a solid presence in Brazil. The Brazilian Institute for Corporate Governance (IBGC) is a non-profit that plays an important role in issuing governance certifications and informing best practices. The Forest Stewardship Council (FSC), created as an initiative for environmental conservation and the sustainable development of forests, and is also a well-recognized source for certifications.

There are also some leading think tanks producing knowledge and providing consultancy on ESG themes, particularly, the Center for Sustainability Studies at Getulio Vargas Foundation (FGVces), the Brazilian Association of Public Companies (Abrasca) and ANBIMA. Public universities, such as the University of São Paulo and the University of Brasília, tend to be valuable information sources, as they contribute most of the academic research produced in Brazil.

13. Has Brazil developed a taxonomy related to ESG?

Brazil has yet to officially adopt an ESG taxonomy. However, many initiatives are currently being undertaken by the private and public sectors in order to develop a national taxonomy standard. In 2020, the Accounting Pronouncements Committee (CPC) issued Technical Orientation No. 9 (OCPC 9), which nationalizes the International Integrated Reporting Council (IIRC) standards for the issuance of Integrated Reporting in Brazil.

In July 2022, the Brazilian Sustainability Pronouncements Committee (CBPS) was created, reflecting the structure of the CPC that is used to adapt the International Financial Reporting Standards (IFRS) on to the Brazilian market. The CBPS is composed by members of Abrasca, Apimec, B3, CFC, Ibracon and FIPECAFI, and is expected to nationalize and standardize the normative issued by the International Sustainability Standards Board.

Despite that Brazilian stakeholders have not reached a consensus regarding acceptable sustainability and related metrics, it is expected that the initiatives developed within the EU will affect the future of taxonomy-related discussions in Brazil. Global companies with activities in the country will likely push for uniformity in the taxonomy considerations to reduce transaction costs of investment in Brazil, and regulators may understand that the developing of an independent taxonomy structure can clash with initiatives developed abroad.

14. What does the future hold for ESG in Brazil?

In the short-term future, it is expected that Brazil will see an increase in ESG-related regulations and laws, as well as the improvement and refining of existing legislation. Regarding environmental practices, it is expected that the market of bonds, assets and services (both regulated and voluntary) will develop, and environmental protection will be pushed forward by financial incentives. It is expected that more institutional investors will start considering ESG indexes and certifications when building their investment portfolios, as data becomes easier to access.

In the medium-term future, in addition to the continuation of the above-mentioned expectations, it is likely that international frameworks will integrate into Brazilian legislation. In the long-term future, it is expected that prioritization of investment in companies with the best ESG practices will be consolidated. The issuing of green bonds and ESG bonds will likely increase. It is also likely that litigation and enforcement activity related to ESG will become more common, and that public companies will expand their role in driving ESG developments.

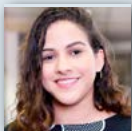
In summary, we expect ESG investment in Brazil to continue growing jointly with worldwide trends. Brazilian society is increasingly demanding accountability from companies in regard to ESG, which will in turn lead to stricter sustainability practices.

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CHILE

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This chapter forms part of:

ENVIRONMENTAL, SOCIAL & GOVERNANCE
Law Over Borders Comparative Guide 2023

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1. How is “ESG” in Chile defined in a corporate/commercial context, and what are its major elements?

ESG is not defined under Chilean Law. Even though several laws and regulations address ESG related matters, specific ESG standards have been included in Chilean regulation only recently.

Under Chilean law, supervised entities (listed companies, securities issuers and entities part of the financial market, including banks, insurance companies, pension fund administrators, among others) must disclose to the public information that would be considered important for the investment decisions of a person of good judgment.

On November 2021, the Chilean Commission for the Financial Market (Comisión para el Mercado Financiero, CMF) issued General Rule No. 461 (NCG 461). NCG 461 sets forth certain ESG related information that must be disclosed by supervised entities starting in end-of-year reports of 2022. This has updated prior instructions relating to social responsibility and sustainable development issued in 2015, which had focused on requiring disclosure of information about diversity and salary breach within regulated entities.

The CMF cited the principles issued by the International Organization of Securities Commissions (IOSCO), such as the importance of ESG disclosure for the transparency of the capital market and the stability of the financial system, for the issuing NCG 461. Accordingly, NCG 461 emphasises disclosure of matters related to corporate governance, the sustainability of the business of the entity, the environment (particularly climate change), social interactions (especially with the relevant stakeholders of the entity), diversity (including the elimination of organizational, social or cultural barriers that may prevent diversity of abilities, conditions, experiences and perspectives from existing within the organization of the entity) and respect for human rights (including eradication of poverty, education for the community and health).

Among other matters, regulated entities must disclose those strategic commitments adopted in furtherance of the Sustainable Development Goals (SDGs) set by the United Nations (UN) or other similar initiatives. Mandatory disclosure is also set out in the Report on the Implementation Strategy in Chile for the UN 2030 Agenda for Sustainable Development, published by the Chilean National Council. This report advises the President of the Republic of Chile and sets out the Chilean Government’s strategy to coordinate public institutions for the fulfilment of the Sustainable Development Goals and the UN 2030 Agenda. According to this report, “investments are only sustainable if they combine the three dimensions of development: environmental, social, and economic. Therefore, sustainable investments include initiatives that can be associated with investments that aim directly at sustainable and inclusive development, that incorporate sustainability criteria (or ESG) or that are capable of measuring, mitigating, compensating and/or reversing their negative impacts”.

2. What, if any, are the major laws/regulations in Chile specifically related to ESG?

The major Chilean specific ESG-related corporate regulations have been issued

by supervising entities of the financial market. The main regulation is NCG 461 and the related guidelines of the CMF regarding the sustainability indicators by type of industry in accordance with the Sustainable Industry Classification System (SICS). Other relevant regulations were issued by the Chilean Pensions Superintendence (SP), on November 2020:

- instructions applicable to Chilean Pension Fund Administrators (AFPs, which manage mandatory pension funds of the Chilean population and are large investment players in the Chilean capital market), establishing the obligation of AFPs to include in their annual reports how climate risks and ESG factors have been considered in the AFP's investment decisions and risk analysis of the long-term sustainability of the securities and markets in which they invest (General Rule No. 276); and
- new parameters for the risk-based supervision model of AFPs, in order to properly identify climate risks and ESG factors in the risk analysis of AFPs (Resolution No. 43).

3. What other laws/regulations in Chile touch on ESG themes?

Aside from regulation of a more general nature – contained, for example, in the Constitution (such as the right to live in an environment free of pollution, the freedom of work, and so on), the International Pact on Economic, Social and Cultural Rights, 49 international conventions of the ILO (International Labor Organization) the Labor Code and Criminal Code – some of the Chilean laws and regulations that, while not specific, relate to one or more aspects of ESG are the following:

- Climate Change Framework Law No. 21,455, Chile's Long-Term Climate Strategy and Chile's Nationally Determined Contributions (2020 updated submission).
- Environment Framework Law No. 19,300 which establishes that certain projects and activities must be previously approved by the environmental impact assessment system (which in some instances will entail mandatory citizen participation).
- Waste Management, Extended Producer Responsibility and Recycling Promotion Law No. 20,920.
- Energy Efficiency Law No. 21,305, which includes a set of measures that aim at reducing energy intensity by 10% by 2030, with an expected cumulative saving of USD 15.2 billion and a reduction of 28.6 million tons of CO₂, as stated by the Ministry of Energy of Chile.
- Green Taxes Law 20,780, establishing an annual tax on air emissions of polluting substances produced by certain types of establishments.
- Criminal Liability of Legal Entities Law No. 20,393 which sets a limited list of crimes that may create criminal liability of a legal entity and includes a cause for exemption in the event that a Crime Prevention Model has been implemented in a timely manner. Currently this list of crimes include the following: money laundering, financing of terrorism, bribery of national or foreign public officials, receiving stolen property, incompatible negotiation, corruption among private parties, misappropriation, wrongful administration,

water pollution, processing of prohibited marine products, illegal extractive activities, overexploitation of hydrobiological resources, infringement of quarantine or isolation measures decreed by the health authority, fraudulent obtaining of unemployment benefits, arms control crimes, human trafficking, cyber-crimes, timber theft and other related crimes.

- The National Decent Work Program, subscribed to by the largest labor union and employers' trade association, emphasizes the eradication of child labor, gender mainstreaming in employment policies, youth employment, occupational health and safety, and education and training.
- Occupational accidents and diseases Law No. 16,744 which establishes the compulsory social insurance covering contingencies such as transitory disability resulting from occupational accidents and diseases.
- Multiple and recent labor laws regarding working conditions which have updated the Labor Code, such as the regulation of remote working, labor inclusion of people with disabilities and work on digital platforms, among others.
- An Association Agreement between the European Union and Chile was recently agreed in November 2022, which will include a chapter regarding sustainable development.

4. What, if any, litigation or enforcement activity has Chile seen related to ESG?

The following are some examples of litigation and public enforcement activity in connection with ESG-related matters:

- From a social perspective, the Labor Department enforces compliance with labor legislation, monitoring and controlling employer's activities and policies. Compliance with labor law is also verified by the labor courts which have the competence to hear all labor matters. From a hygiene and security at work point of view, the Ministry of Health has the authority to control the fulfillment of the legal obligations established to ensure safety conditions at work.
- In a citizen promoted litigation, the Supreme Court has ruled that the guidelines and principles related to sustainable development should have been considered in the environmental assessments of projects and activities (*Jara Alarcon Luis v. Servicio de Evaluación Ambiental* (2019)).
- Consumer Protection Law includes possible sanctions for misleading advertising of products. The development of greenwashing may lead to enforcement action under this law.
- Governmental environmental authorities encouraged the industry to stop producing single-use plastic products by issuing voluntary stamps such as "Bye-Plastic Bags" and "Bye-Plastic Drinking Straws". These initiatives were codified, and the supply of single-use plastics to consumers is now banned (Laws No. 21,100 and 21,368).
- In 2008, the General Electric Services Law introduced a quota for generators to source at least 10% of their annual energy usage from Non-Conventional Renewable Energy (NCRE). The 10% quota was managed easily, and in 2013

was increased to 20% (as of August 2022, 34.4% of net capacity is sourced from NCREs).

- In 2021, the National Electric Coordinator launched a blockchain renewable energies registry (RENOVA platform), with the goal of providing a traceable and unalterable record of each megawatt hour of renewable energies to enable generators and users to verify its origin and delivery.

The following are examples of private initiatives and enforcement activity:

- The Council for Self-Regulation and Advertising Ethics (CONAR) has produced the Code of Advertising Ethics, which includes regulations regarding advertising related to the environment, and has ruled on cases of greenwashing.
- Voluntary industry-sector Clean Production Agreements entered into by private companies with Governmental authorities, which were registered in the UNFCCC Secretariat's Nationally Appropriate Mitigation Actions (NAMAs) registry.
- More than 100 Certified B Corps (with headquarters in Chile) have voluntarily agreed to implement specific provisions on stakeholder governance, environmental, workers policies, community and customers in their bylaws to meet the legal requirement for B Corp Certification.
- The Ministry of Energy has developed an Energy Roadmap for 2018-2022, which includes the gradual phase-out of coal-fired power plants that do not have carbon capture and storage systems or other equivalent technologies (the Decarbonization Plan). Pursuant to this plan, the Ministry of Energy entered into agreements with relevant energy companies to retire coal-fired thermal power plants.
- The Ministry of Labor and Social Security established a 40-hour Certificate for employers who have voluntarily implemented a reduction of their weekly working hours.

5. What are the major non-law/regulatory drivers of ESG trends and developments in Chile?

Soft non-binding laws

Chilean authorities have promoted the following soft non-binding laws:

- The UN SDGs and the 2030 Agenda for Sustainable Development. According to the 2022 Sustainable Development Report, Chile is on track or maintaining achievement of SDG No. 1 (No Poverty), No. 6 (Clean Water and Sanitation), No. 7 (Affordable and Clean Energy), No. 11 (Sustainable Cities and Communities) and No. 17 (Partnerships for the Goals).
- The UN Guiding Principles of Business and Human Rights.
- OECD Guidelines for Multinational Enterprises.
- 9 out of 10 of the International Labour Organization's fundamental conventions including the Forced Labour Convention (No. 29).
- OECD Guidelines on Corporate Governance of State-Owned Enterprises.
- Public procurement guidelines for state agencies incorporating environmental and energy efficiency criteria issued by the procurement state agency Chile Compra.

Stakeholders

Stakeholders that promote the consideration of soft-law or ESG in general:

- More than 100 companies are members of the UN Global Compact's Chilean Network. The top sectors of these members are food production, electricity, mining and financial services.
- Up to August 2022, 29 Chilean companies from various sectors (food and beverage, infrastructure, financial, mining, transportation, renewable resources and alternative energy, among others) reported using the Sustainability Accounting Standards Board (SASB) Standards.
- The State of Chile has issued sovereign Green Bonds structured in accordance with Chile's Green Bond Framework prepared by the Ministry of Finance and the support of the Inter-American Development Bank. Proceeds are used to finance public projects such as clean transportation, energy efficiency, renewable energies, live natural resources, water management and green buildings.
- Banco Estado (state-owned bank) has issued green financial instruments, such as loans for NCRE projects, mortgages for ecological housing and clean transportation loans.

National Contact Points (NCPs)

Some National Contact Points active in ESG matters in Chile are the following:

- UN Global Compact's Chilean Network. See pactoglobal.cl.
- Chilean OECD National Contact Points for Responsible Business Conduct. See www.subrei.gob.cl/ejes-de-trabajo/ce/punto-nacional-de-contacto.
- Chilean Universities:
 - Vincular Corporate Sustainability Center of the School of Business and Economics of the Pontificia Universidad Católica de Valparaíso (PUCV). See www.pucv.cl/uuaa/site/edic/base/port/vincular.html.
 - Corporate Sustainability Programme of the Law School of the Pontificia Universidad Católica de Chile (PUC). See sostenibilidadcorporativa.uc.cl.
 - PUC's Corporate Governance Center. See centrogobiernocorporativo.uc.cl.
 - ESE Business School of the Universidad de Los Andes. See www.ese.cl.
- State's institutions:
 - National Council for the Implementation of the 2030 Agenda. See www.chileagenda2030.gob.cl.
 - Preliminary Green Taxonomy Committee of the Ministry of Finance and other authorities. See www.hacienda.cl.
 - Energy Sustainability Agency. See www.agenciase.org.
 - Sustainability and Climate Change Agency. See www.ascc.cl.
 - Office of Circular Economy of the Ministry of the Environment. See mma.gob.cl/economia-circular.
- "Sistema B" NGO. See www.sistemab.org.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

Yes, those regulations are related to corporate disclosure.

Reporting

- NCG 461 provides that annual reports of regulated entities must contain ESG related information such as:
 - The strategy relating to environmental aspects, with special attention to climate change issues and compliance with the strategic commitments adopted within the framework of the UN SDGs.
 - Sustainability metrics that are relevant according to its industrial sector pursuant to the Sustainable Industry Classification System (SICS) and the definition of metrics under the Sustainability Accounting Standards provided by SASB.
- NCG 276 establishes that the annual reports of AFPs must expressly mention the treatment of credit and market risks, climate risk and ESG factors.
- The Sustainability Reporting and Disclosure Guidelines for Issuers in the Chilean Stock Market of the Santiago Stock Exchange and the Global Reporting Initiative are a resource for companies to comply with NCG 461 and NCG 276.

7. Which sectors are most impacted by ESG in Chile? How significant is ESG investment in Chile?

- Large companies of several sectors (food producers, electricity, mining, financial services, transportation, renewable resources and alternative energy and resource transformation) are impacted by ESG initiatives.
- More than 100 companies with headquarters located in Chile are certified as B Corp companies.
- According to the 2021 Ipsos Climate Change + Consumer Behaviour survey in Chile, 24% of those surveyed stated that they have made a lot of changes in their consumption behavior out of concern about climate change, and 49% stated that they have made a few changes.
- Under the Extended Producer Responsibility Law companies that produce “priority products” (such as tires, containers and packaging, batteries and electronic items, and lubricating oils) must organize to implement and finance individual or collective management systems that allow them to comply with waste management goals.
- Under the Energy Efficiency law, companies with an energy consumption for final use of over 50 tera-calories in the previous calendar year are Energy Management Capable Consumers, who must submit an energy management plan to the authority.
- Under Labor Inclusion Law No. 21,015, employers with more than 100 employees must comply with the inclusion of people with disabilities in the labor market (through a hiring quota for people with disabilities or with two possible alternatives to comply in the event of unsuccessful searches for applicants for the workplace: (i) donations to an NGO’s project or activity for people with disabilities; or (ii) entering into service contracts with companies that employ people with disabilities).

Hedge funds/asset managers

AFPs are required to comply with NCG 276 of the SP.

Banks

The Chilean Central Bank in its most recent Financial Stability Report has highlighted the challenges that climate change may have for the stability of the financial system and has outlined a work agenda to face those challenges. In addition, many banks have voiced that they have incorporated sustainability indicators and climate change into their credit policies and sustainability-linked loans.

Fashion

The Ministry of the Environment announced that it will strive for the amendment of the Extended Producer Responsibility Law to include textile products as a priority product to combat clothing dumping and other illegal actions.

Automobile industry

In 2013, Chile became the first Latin-American country to introduce a mandatory energy efficiency labeling for motor vehicles. In February 2022, the Ministry of Energy issued a new regulation setting minimum energy efficiency performance levels for new vehicles commercialized by the automobile industry starting from 2024. The relevant metric to define the new standards will be energy yield in kilometres per liter of petrol.

Energy industry

Under the Decarbonization Plan, main power generators entered into agreements with the Chilean government for the decarbonization of the energy matrix. In addition, energy generators have modified their project portfolios due to the lower cost and technology improvements of NCRE projects, bottlenecks following the delays in the construction of extensions and modifications to the National Electric Grid, and the decrease in hydropower production due to the water drought. The State and the private sector are promoting a campaign for the production and use of green hydrogen.

Real estate industry

The Energy Efficiency law establishes that new residential, public, commercial and office buildings must have an energy efficiency label and rating report in order to obtain the definitive building approval.

E-commerce

The CONAR's Chilean Code of Advertising Ethics includes regulations regarding advertising related to the environment.

In 2021, the Ministry of Economy issued Decree 6/2021, setting forth an e-commerce regulation aimed at strengthening the transparency and quality of information provided to consumers.

8. What are the trends in Chile regarding ESG governance?

Corporate disclosure

Several large Chilean companies are publishing sustainability reports and some have set up specialized teams in sustainability and corporate affairs matters. However, NCG 461 and NCG 276 are a bigger challenge for companies that had not invested so far in these matters.

According to the preliminary results of a 2021 survey to companies' directors and CEOs carried out by Los Andes University, more than 50% of the surveyed did not have experience regarding ESG topics, but indicated that their companies were making efforts to implement ESG metrics and were starting to hire ESG specialists and creating stronger sustainability departments to respond to stakeholders' demands, comply with regulations and closing gaps with competitors on ESG matters.

Compliance

Since the enactment of Law 20,393 on Criminal Liability of Legal Entities in 2009, and especially during the last few years, there has been significant progress and development of the compliance area within companies.

Although in Chile it is not legally mandatory to have a Crime Prevention Model or compliance policies in place, in practice the lack of such Model is considered by criminal courts as a breach of the general duties of care within the company when a crime is committed. For that reason, it is common for medium to large size companies as well as those most exposed to risk, to have and implement such policies and to designate a compliance officer for the company, either because they seek to maintain a high standard of compliance or to comply with the international standards of their international parent companies.

As a result, companies with a more sophisticated governance have started to introduce ESG-related activities and issues into the organization as part of their compliance programs. Specifically, to their training plan, communication guidelines, as well as to their monitoring and risk management plan.

9. To what extent are ESG ratings or ESG benchmarks relied upon in Chile?

ESG rating agencies

The first ranking of the Corporate Reputation Business Monitor (Merco) for Chile was published in 2022, listing 100 Chilean companies in a general ESG ranking and in sub-rankings for each ESG aspect. Merco states that the three key variables for considering a company to be ESG responsible are ethical behavior, transparency and good corporate governance, and responsibility towards its employees.

The Federation of Chilean Industry (SOFOFA) published in September 2022 the general results of their ESG SOFOFA 2022 index with more than 55 companies. See sofofa.cl/ejes-estrategicos/desarrollo-empresarial-sostenible/esg.

ESG benchmarks

The following ESG benchmarks are used in the Santiago Stock Exchange:

- Dow Jones Sustainability MILA Pacific Alliance Index, which tracks the performance of companies with the highest sustainability ratings for the Pacific Alliance region, including Chile, Colombia, Mexico and Peru.

- Dow Jones Sustainability Chile (DJSI Chile) Index, which uses the “best-in-class” approach representing the top 40% of the Santiago Stock Exchange’s General Share Price Index based on long-term environmental, social and governance factors.
- S&P IPSA ESG Tilted Index, which follows selection criterion based on ESG principles.
- Stakeholders Sustainability Index Chile (SSIndex), which provides an ESG map risk with a cross-analysis of ESG information from employees, clients, suppliers, communities, and investors.

10. What is the role of the private markets versus public markets in driving ESG developments in Chile?

ESG developments and the ESG agenda have progressed by a combination of public and private initiatives.

In addition to the issuance of the Report on the Implementation Strategy in Chile for the UN 2030 Agenda for Sustainable Development discussed above, in December 2019 the Minister of Finance, with the support of the Ministry of the Environment, presented a voluntary Green Agreement between the government, regulators (CMF, Central Bank, SP, Inter-American Development Bank representatives in Chile, and Banco Estado) and private actors in the financial sector. This agreement aims to contribute to financial stability and the achievement of Chile’s climate commitments.

In addition, the ESG agenda has been driven by international organizations. For example, as a member of the OECD since 2010, Chile should follow the conclusions of the OCDE’s report regarding the future of corporate governance in capital markets following the COVID-19 crisis and improve its management of ESG. This OECD report concludes that ESG disclosure frameworks will also help the corporate sector meet increased expectations when it comes to recognizing and appropriately balancing the interests of different stakeholders, including investors, employees, creditors, customers and suppliers, and their contribution to the long-term success of corporations, and recommends measures for companies, policy makers and regulators, and corporate boards.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

Some of the major challenges in terms of complying with ESG obligations for Chilean companies are the following:

- Investment in ESG specialized teams.
- Establishing labor policies that promote health and quality of life at work.
- Training the board members, executives and workers in ESG matters.
- The implementation of new reporting regulations (NCG 461 and NCG 276, as applicable) and other regulation, such as:
 - the waste management systems required by the Extended Producer Responsibility Law;
 - the new e-commerce regulations; and
 - other measures to avoid greenwashing and meet consumers’ demands.

- The implementation of the Chile's NDC that may result in the shutdown of highly polluting industries and projects (e.g., through the Decarbonisation Plan described above) that currently provide many direct and indirect jobs to local communities.
- The implementation of new technologies for the energy transition, such as storage systems and green hydrogen projects, considering current infrastructure limitations and constantly evolving regulation (e.g., a regulation on sufficiency capacity is underway, which is expected to have an impact in achieving clean energy goals).

12. What information sources are most relevant for ESG considerations in Chile?

As mentioned above, the main sources are university centers, business associations and state organizations. Furthermore, an important source of information has been the Chilean companies' sustainability reports.

13. Has Chile developed a Taxonomy related to ESG?

Not yet. However, in May 2021, the Ministry of Finance and the Climate Bonds Initiative published a "Taxonomy Roadmap for Chile" report with the support of the International Climate Initiative (IKI). In June 2022, a Preliminary Committee on Green Taxonomy started to work.

14. What does the future hold for ESG in Chile?

In the short to medium term, regulated entities will face the challenges in implementing the new mandatory ESG disclosure regulations. This could pose a bigger challenge for companies that have not yet invested in ESG matters.

In the medium to long term, we may see different actors work to improve their ESG performance and align their internal goals with sustainable development. We may also see the development of a Chilean taxonomy. These efforts will probably be driven by the need to adapt to the effects of climate change, the oversight and regulation of the competent authorities, the community's opinion, consumers preferences, and the expectations of shareholders and investors in respect of greater profits for companies that contribute with a sustainable development approach.

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CHINA

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1. How is “ESG” in China defined in a corporate/commercial context, and what are its major elements?

ESG in China, despite not being officially defined in statutory laws and regulations, is comprised of three inherent elements: environmental protection, social responsibility and corporate governance. Though consideration of ESG factors existed in many forms before it garnered much attention, the practice grew in popularity among investors and legal practitioners in China when the “dual carbon” goals were recognized. In the last couple of years, the government and companies have mainly been focusing on the reduction of carbon emission when they consider ESG.

2. What, if any, are the major laws/regulations in China specifically related to ESG?

In China, major laws specifically related to ESG mainly focus on environmental protection. They are:

- Environmental Protection Law (Amended in 2014);
- Environmental Impact Assessment Law (Amended in 2018);
- Law on Prevention and Control of Atmospheric Pollution (Amended in 2018);
- Law on Soil Pollution Prevention and Control (Enacted in 2018);
- Law on Prevention and Control of Water Pollution (Amended in 2017); and
- Work Safety Law.

There are also other relevant regulations that touch upon ESG themes, such as regulations issued by the China Securities Regulatory Commission (CSRC) and regulatory agencies such as the stock exchanges.

3. What other laws/regulations in China touch on ESG themes?

The following laws also touch on ESG themes:

- Company Law;
- Criminal Law;
- Labor Law;
- Labor Contract Law;
- Antitrust Law;
- Anti-Money Laundering Law
- Anti-Unfair Competition Law;
- Law on the Protection of Rights and Interests of Women; and
- Law on the Protection of Minors.

For example, the Anti-Unfair Competition Law requires business operators to assume social responsibilities. When participating in production and business activities, they must not take illegal measures, such as offering bribes to disrupt the order of market competition, or to undermine the legitimate rights and interests of consumers or other operators.

The Antitrust Law also aims at improving social benefits by preventing adverse impacts arising from monopoly, and, providing a good environment for innovation and consumer protection, which contributes to the sustainability of the economy and society of China.

4. What, if any, litigation or enforcement activity has China seen related to ESG?

Enforcement in relation to ESG is comprised of a wide range of actions within different legal departments as there is no consolidated legislation on ESG. Some major cases in China were in breach of Antitrust Law, which touches on themes falling within social responsibility. In 2021, The Anti-monopoly Bureau of the State Administration for Market Regulation imposed a CNY 18 billion fine on Alibaba for its monopoly in the online retail business and, in the same year, imposed a CNY 3 billion fine on Meituan for using platform algorithms to impose discrimination measures on those who cooperated with competitors.

Enforcement actions for environmental protection also regularly occur. For example, in 2020, Jinyuanli Chemical Co., Ltd., was fined CNY 150,000 by Changji Ecological Environment Bureau following harmful gas emissions.

5. What are the major non-law/regulatory drivers of ESG trends and developments in China?

Soft non-binding laws

In 2018, the CSRC revised the “Governance Guidelines for Listed Companies”, stipulating that listed entities have a responsibility to disclose ESG information. They deemed “sustainable development” and “green development” to be the guiding principles for the companies to consider.

Following that, the Asset Management Association of China released the “Green Investment Guidelines” and “ESG Evaluation System of Listed Companies in China”.

Stakeholders

The government, as an important stakeholder, is proactive in the promotion of ESG. In 2020, President Xi Jinping promised the world at the 75th United Nations General Assembly to “make efforts to achieve carbon peak by 2030, and make efforts to achieve carbon neutrality by 2060”. This “dual carbon” goal was officially written into the “Government Work Report”, which has prompted more companies to pay attention to the issues of ESG and study the impact of ESG on their business operations, in order to get more favorable treatment from the government.

However, the requirements to release ESG related data or disclose their ESG reports to the market without specific guidelines has caused an increase in greenwashing. Greenwashing has become a concern for the industry in China, but there is still a lack of laws or regulations to fundamentally prevent greenwashing.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

Yes. There are some statutory obligations for disclosure. For example, the “Environmental Impact Assessment Law” requires companies’ prior disclosure about their planning when they intend to start construction, add more production lines or increase the capacity of the existing facilities. Additionally, the “Work

Safety Law” requires companies to disclose to the relevant government authority any potential hidden dangers found during the companies’ regular inspections.

Reporting

Some listed companies or other large companies may voluntarily choose to disclose an annual ESG report and the government and stock exchanges encourage companies to do the same. These ESG reports can be usually found on the investor relationship webpage of the companies’ official websites, and, for companies listed in China, they may disclose the reports in the form of a public company announcement through the stock exchanges. However, there are no standard metrics, accounting mechanics or frameworks which are consistently used in these voluntary disclosures.

Notably, legislators and regulators are considering the compulsory disclosure of ESG reports, and the Shanghai Stock Exchange requires the companies listed on the STAR MARKET to comply with the obligation to disclose an ESG report.

7. Which sectors are most impacted by ESG in China? How significant is ESG investment in China?

Private equity

The Asset Management Association of China released the “Green Investment Guidelines” and the “ESG Evaluation System of Listed Companies in China” in 2018, which requires the mutual funds and private equity funds investing into securities to follow the Green Investment Guidelines to formulate their internal green investment policy, set up certain positions and employ analysts to have in-depth analysis on the green investment targets, and, submit self-evaluation forms on their managerial and policy adjustment, as well as the performance of green investment. Private equity funds investing into private company equities can choose to follow the above guidelines. Recently several private equity fund management companies have established their ESG compliance program in accordance with the above guidelines.

Real estate industry

Real estate companies have far greater capacity to impact the environment due to the nature of their business. Their ESG reports suggest that they have directly improved the means of their business ventures to better suit modern sustainability expectations by developing their environmental standards and driving building renovations into impoverished communities. Vanke, one of the largest real estate companies in China, is an example of this. Vanke decided to collaborate with nature in their projects by promoting the practice of “green building”, by formulating a “green standard” scale where projects can be star rated by their fulfillment of the goals of “green building”. By using sustainable materials that do not degrade the environment and by incorporating elements of nature in their projects, Vanke has come up with interesting pieces of architecture such as the Mega Eco Botanical Garden in Shanghai. Furthermore, not only is “green building” reintroducing nature back into cities, it is also a system that encourages sustainable energy sources.

E-commerce

In China people rely heavily on e-commerce. The e-commerce companies in China are also commercial giants with huge capital to make investment. As a result, e-commerce companies can have a great impact on ESG by bringing attention to it when guiding consumers, allocating internet traffic, and making investments. For example, JD.com, one of the largest e-commerce platforms, has developed governance structures, which divide responsibilities into decision-making and execution teams. Notably, JD.com hires experts from various fields and employs current members of the company in order to define objectives, execute initiatives, and collaborate with investors to better the impact of a company's ventures.

Other examples are e-commerce food delivery platforms such as Meituan and Ele.me. Meituan launched the "Green Mountain Scheme" in 2017, which is an action for protecting the environment. It aims at making progress to reduce the waste generated from food delivery and its packaging, by investing in R&D in this regard and working together with government departments, professional institutions, experts and scholars. Ele.me has made some efforts in social responsibility, by exploiting their advantages as a platform. For example, Ele.me cooperates with the consumers, charities and some of the in-platform restaurants and cafes to build up a community; consumers can find those restaurants and cafes with the "love" tag, and a part of money they spent in these restaurants and cafes will be donated to support children in rural areas to get enough and healthy food.

Game industry

The gaming industry is kept alive by fostering a competitive but non-toxic atmosphere for consumers. One of the greatest hindrances to this ideal is the expression of insults and slurs in games or the game-community. Tencent, as the largest game company in China, tackles this issue by promoting healthy games implementing a real-name system along with an anti-addiction system in accordance with regulatory requirements. Such a system links one's online persona to their physical one and suggests implications for breaking in-game regulations. Furthermore, even more regulations are created for minors to regulate their experiences in games and the game community. Namely, systems are put in place to allow parents more moderation over children's purchases and screen time. Although these measures may restrict Tencent and other game companies from earning more money, these constraints are part of their social liabilities.

8. What are the trends in China regarding ESG governance?

With strong public encouragement, large corporations have implemented ESG governance. In the case of Tencent, an ESG working group directly led by the Board of Directors was launched to carry out ESG related matters. Similarly, as mentioned above in Question 7, JD.com, one of the largest e-commerce platforms, also developed ESG governance structures, which divided responsibilities into a decision-making and execution teams. Notably, JD.com hires experts from various fields and employs current members of the company to define objectives, execute initiatives, and collaborate with investors to ensure that the company's business

and investments are making better impact. Other leading companies in China follow suit and have been developing their own ESG management program.

In some finance institutions in China, the role of a Chief ESG specialist has become extremely important. For example, Ping An Bank has implemented a thorough managerial and strategic mechanism to improve ESG related performance and to ensure sustainability. Notably, Ping An Bank has a Chief ESG specialist and a team specializing in ESG, which contributed to Ping An Bank's award of "Best ESG" (awarded by the Institutional Investor magazine, 2022).

9. To what extent are ESG ratings or ESG benchmarks relied upon in China?

ESG rating agencies

It is generally investors who use ESG rating agencies to evaluate the ESG performance of an investment target, in order to decide whether they should take a step further and make an investment. In China, the leading international ESG rating agencies' ratings and reports are commonly accepted by investment managers or finance institutions when they evaluate a company's ESG performance, such as MSCI ESG, S&P ESG Index, Bloomberg and Morningstar. At the same time, several other rating agencies, such as Wind ESG Rating and Sino-Securities ESG Rating, have been providing ESG ratings covering most A-share Listed companies. Companies rarely directly engage with ESG rating agencies, however, companies (especially listed companies and large companies) may meticulously prepare their ESG related information to feed the ESG rating agencies, in order to improve their own ESG ratings.

ESG benchmarks

ESG benchmarks like MSCI World SRI Index or Sustainalytics ESG benchmarks are usually used by mature institutional investors during their decision making of ESG related investment. Some of these published ESG benchmarks may be used as a reference by investment institutions or finance institutions when they formulate their internal ESG benchmarks.

10. What is the role of the private markets versus public markets in driving ESG developments in China?

Private companies

Usually, private companies might focus on developing an environmentally friendly supply chain as their "selling point" to attract consumers and investors. Private companies planning to go public may emphasize their ESG performance so as to build up an advantage in attracting international funding and make early preparation for any future listing. For example, in April 2021, Cainiao Guoguo (a courier company mainly distributing online shopping parcels) launched an environmental protection event called Ocean Parcel That Cannot Be Refused. During this event the participants received parcels for free, but were shocked to find that they contained only plastic bottles, bags and straws, together with a letter. In this letter, Cainiao Guoguo provided data about the polluted ocean, and reminded the recipients to protect the ocean by reducing waste. This event

turned out to be a great success for Cainiao Guoguo, greatly improving its brand reputation. Some investors believe this is a step taken by Cainiao Guoguo for attracting more attention from investors and preparing for its public offering in the future.

Public companies

Some state-owned public listed companies are proactive in making positive responses to ESG issues and in several industries, such as electric power, coal, dairy and liquor, ESG ratings of state-owned public listing companies are higher than private listed companies'. State-owned public listed companies are, to some extent, the pioneers echoing national policies, such as "dual carbon", energy and resources conservation, compliance discharge of pollutants, product safety and quality as well as protection of labor rights and interests, which are also the highlighted focus of ESG.

Beyond ensuring regulatory compliance, we've observed activities of some public companies who are proactive in developing approaches to ESG issues. For example, some are making donations to charities or schools at areas of poverty, and, others are designing buildings or developing building materials which are energy-saving. These actions go way beyond regulatory compliance.

Public companies and private companies may address ESG issues in their disclosure and also in their products and services, to attract consumers and investors. However, we've not seen publicly discussed cases of divestment purely for bad ESG performance in particular.

ESG agenda

No official regulation or policies relating to ESG agenda implementation have been observed in China. Which means the enterprises may voluntarily set up an ESG agenda, but it's not compulsory and the government will not monitor the enterprises on this. However, in March 2022, State-owned Assets Supervision and Administration Commission under the PRC State Council established the Social Responsibility Bureau, whose responsibility is encouraging companies, especially state-owned companies to actively put ESG into practice. It is also an unofficial signal implying that the ESG agenda has become more popular and will become a tendency for all companies.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

Given China is still in its initial stage of ESG integration, companies are facing significant challenges. Considering the impact of the COVID-19 pandemic and the downturn of the economy, commercial benefit has been positioned as the primary target by most companies. Under this economic pressure, companies may trade off the ESG compliance for boost in output.

However, since the implementation of the "dual carbon" goals, companies are also faced with pressure from a regulatory perspective. Companies falling under "upper limit" policy (i.e., for enterprises that have not conducted the actual measurement of elemental carbon volume in coal in 2019, the carbon volume in

unit heating value shall be calculated at 33.56tC/TJ) would afford more carbon emission after calculation, and these companies may consider circumventions of the above consequence and may end up with data fraud.

Nevertheless, regulation has reinforced the supervision of data disclosure, such as environmental data. Administrative Measures for the Mandatory Disclosure of Environmental Information by Enterprises was promulgated on December 11, 2021 by the Ministry of Ecology and Environment and took effect on February 8, 2022, specifying the content, form and timing of disclosure by the companies with great environmental impact and high public concern and related supervision measures with penalties if companies fail to comply. The above measures are aimed at preventing data fraud and greenwashing in sustainability statements. With these mandatory regulatory requirements for disclosure, companies may have to set up specific positions or may have to purchase and install certain devices in order to get prepared for data reporting, which may increase the companies' costs in a short term.

12. What information sources are most relevant for ESG considerations in China?

Normally, aside from the information acquired from self-disclosure by the enterprises, such as annual reports, ESG reports, Company Social Responsibility reports (CSR report) and announcements by listing company, information acquired from NGOs, academics, government, news and social media is also important for reference. Among others, in China, statistics disclosed by NGOs constitute an important ESG consideration. The Institute of Public and Environmental Affairs (IPE), a non-profit environmental research organization registered and based in Beijing, has built a database of environmental information – Blue Map website – collecting, collating and analyzing government and corporate environmental information, including environmental monitoring data. However, the data acquired from NGOs shall be cleaned and deduplicated before being taken into account for the ESG rating.

13. Has China developed a Taxonomy related to ESG?

In July 2020, coordinated by the International Platform on Sustainable Finance (IPSF), the EU and China initiated a Working Group on Taxonomies with the objective to undertake a comprehensive assessment of the existing taxonomies for environmentally sustainable investments, including identifying the commonalities and differences in their respective approaches and outcomes. In November 2021, the IPSF Taxonomy Working Group published the first version of the Common Ground Taxonomy (CGT) report, and, issued a call for feedback to solicit comments. After that there was a second version of the CGT report. At this stage the CGT report is only a draft of the overview between the EU and China taxonomies within the scope of the instruction report with no legal effect and is not formally endorsed by IPSF member jurisdictions. The result does not create either a common or single taxonomy or a standard that is mandatory for IPSF member jurisdictions.

To our knowledge, there is no ESG related Taxonomy published within the jurisdiction of China yet. Some finance institutions may have developed their own standard to classify clients or targets from an ESG perspective.

14. What does the future hold for ESG in China?

As ESG is still a new topic in China, it is attracting companies' and investors' attention. In the short term, ESG will continue to play a role in the market value management of large companies as a tool to convince investors that the companies are paying attention to good governance, sustainability and so on, in order to increase the share price.

In the medium term, we are expecting a more standardized matrix for ESG related disclosure, evaluation, financing and investment. Once this happens, ESG performance may become an index like credit scores; on the other hand, banks, insurance companies, investors and regulators may have developed precise measures to prevent greenwashing or similar tricks. Consumers and investors may develop a more comprehensive understanding of ESG, impacting their choice when they purchase products or invest into companies or projects which are highlighting their good ESG performance. They will be more cautious about the price mark-up driven by the ESG costs or even only by the ESG concepts.

In the long run, good governance may maintain company stability. Improvement in environmental protection may in return drive the companies to explore more energy saving technologies in their production and which may also save costs in the long run; and, proactively taking on social responsibilities may improve the companies' image and win trust from consumers, investors and regulators, which will also help companies win market shares and create a good environment for financing. We remain positive for the future of ESG in China.

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Mr. Gary Gao is the Partner and Head of Compliance & Regulatory Department of Zhong Lun Law Firm. Before being admitted to the PRC Bar in 1995, Mr. Gao worked as a judge in a district court in Shanghai from 1990. Mr. Gao has practiced as a lawyer for 27 years, and is highly experienced in both compliance & regulatory as well as international dispute resolution. He has a full understanding of the entire operation of these enterprises, which in turn helps clients to succeed.

Mr. Gary Gao has made persistent efforts in the frontiers of the legal profession, including with ESG compliance and law matters. He has served many leading companies in China to develop their internal ESG compliance program and management mechanism, publish their ESG report to the public or submit the ESG report to the regulators, and, deploy ESG matrix into many investment companies' / asset managers' investment process and tools. Notably, besides Chinese ESG laws and practices, he also coordinates with many overseas legal professionals and assists Chinese companies to improve their ESG performance and reduce ESG related risks during their overseas business activities.

EUROPEAN UNION

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1. How is “ESG” in the European Union (EU) defined in a corporate/commercial context, and what are its major elements?

The EU has not adopted a formal definition of “ESG”. The EU has, however, adopted similar concepts around “sustainability”, as discussed below.

2. What, if any, are the major laws/regulations in the EU specifically related to ESG?

The impetus for ESG regulation in the EU can be traced back to a series of landmark international agreements concluded in 2015, namely the adoption of the UN 2030 Agenda for Sustainable Development and its Sustainable Development Goals and the Paris climate agreement. The latter includes a commitment to align financial flows with a pathway towards low-carbon and climate-resilient development.

The European Commission’s 2018 Action Plan on Financing Sustainable Growth identified 10 key action points to fulfil these sustainability goals in respect of financial services, including:

- establishing a taxonomy for sustainable activities;
- creating standards for “green” financial products;
- incorporating sustainability as part of financial advice;
- developing sustainability benchmarks and improving the integration of sustainability within ratings; and
- strengthening disclosures made by asset managers and financial advisers to their clients.

Moreover, in December 2019, the Commission presented the European Green Deal (Green Deal), a growth strategy aiming to make Europe the first climate-neutral continent by 2050. To this end, the Commission has been developing a comprehensive policy agenda on sustainable finance in the framework of the Green Deal and the new strategy for financing the transition to a sustainable economy.

Corporate Sustainability Reporting Directive (CSRD)

In a bid to extend the scope of, and address shortcomings in, the Non-Financial Reporting Directive (NFRD), the European Parliament formally adopted the CSRD in November 2022, which establishes a new mandatory framework for non-financial disclosures in the EU. The requirements will apply to all large EU companies that meet certain financial thresholds, listed or otherwise, as well as non-EU companies with turnover of at least EUR 150 million in the EU. The CSRD amends several existing directives such that nearly 50,000 companies will be subject to the new reporting obligations, compared to approximately 11,700 under the current regime. Reporting requirements under the CSRD will apply on a phased basis, as follows:

- from January 1, 2024, for large public interest companies with over 500 employees that are already subject to the NFRD;
- from January 1, 2025, for large companies not currently subject to the NFRD (over 250 employees and/or EUR 40 million in net turnover and/or EUR 20 million on its balance sheet); and

- from January 1, 2026, for listed small and medium-sized enterprises (SMEs). SMEs can opt out until 2028.

The CSRD envisages the adoption of EU Sustainability Reporting Standards (ESRS), to be developed by the European Financial Reporting Advisory Group (EFRAG). EFRAG has published a first set of draft ESRS, which were submitted to the Commission on November 22, 2022, and is currently in the process of developing sector-specific standards in addition to those aimed specifically at SMEs.

Sustainable Finance Disclosure Regulation (SFDR)

The EU's SFDR entered into force in December 2019 and requires all EU financial market participants and financial advisors (including non-EU firms marketing in the EU) to make ESG disclosures in relation to their financial products, sustainability risks and adverse sustainability impacts. The scope of required disclosure depends on the level of integration of ESG considerations within the financial product. Products promoting environmental or social characteristics (Article 8 products) and products having sustainable investments as their objective (Article 9 products) are subject to pre-contractual and ongoing disclosures on sustainability indicators used to monitor performance. The SFDR's Level 1 requirements have been applicable since March 2021. The final Level 2 disclosures were published in the Official Journal of the EU in July 2022 and apply from January 2023.

Level 1 entity-level disclosures require fund managers to:

- assess the potential for ESG factors to negatively impact the returns of funds under management; and
- disclose the outcome of that assessment to investors both in funds' prospectus documents and on the firm's website.

The entity-level disclosures also require in-scope firms to publish an "adverse impacts statement" on their website. Firms with 500 or more employees are required to publish a statement describing the due diligence policies that are applied by the firm to identify the adverse impacts of investment decisions on sustainability factors. Firms with fewer than 500 employees have the option to either publish a statement or clearly state that adverse impacts are not taken into account (as long as they detail why they are not and, where relevant, whether there is an intention to account for them in the future).

Level 2 product-level disclosures include pre-contractual and periodic disclosure templates for Article 8 and Article 9 products, which should be annexed to prospectuses and annual reports, as well as a principal adverse sustainability impacts statement template. Such disclosures now play a big role in new marketing activities, including by private fund managers.

Taxonomy Regulation

The Taxonomy Regulation, as applicable from 1 January 2022, sets out a common set of technical screening criteria to test and measure the extent to which an economic activity qualifies as environmentally sustainable. It applies where financial market participants make products available that promote specific environmental characteristics or products that have sustainable investment as an objective.

In order to align with the regulation and qualify as environmentally sustainable, the activity must substantially contribute to at least one of the six environmental objectives and comply with the relevant technical screening criteria. It must do no significant harm to any other environmental objective and must comply with minimum safeguards. The six environmental objectives are:

- climate change mitigation;
- climate change adaptation;
- sustainable use and protection of water and marine resources;
- transition to a circular economy;
- pollution prevention and control; and
- protection and restoration of biodiversity and ecosystems.

Under Article 8 of the regulation, firms subject to the NFRD, as described below, are required to disclose the proportion of turnover derived from products or services that qualify as environmentally sustainable, and the proportion of the capital and operating expenditure relating to assets or processes associated with those activities.

The regulation initially focused on climate change issues, with technical screening criteria and disclosure requirements applicable to the objectives of climate change mitigation and adaptation applying from 1 January 2022. In March 2022, the Commission's Platform on Sustainable Finance published its recommendations for technical screening criteria for the remaining four objectives.

While the Taxonomy Regulation is concerned with the measurement of the environmental sustainability of certain economic activities, the Commission is also considering the establishment of a social taxonomy. As discussed in more detail below, this is expected following the end of the Commission's current mandate in 2024.

Non-Financial Reporting Directive (NFRD)

In relation to non-financial reporting, the NFRD applies to large public-interest entities (such as companies listed on a regulated market of any Member State, credit institutions, insurance undertakings and those designated as public-interest entities by Member States) with over 500 employees during the financial year as recorded on their balance sheet. The directive requires those companies, along with public-interest parent companies of large groups that collectively employ more than 500 people, to include a non-financial sustainability statement within their management report. This provides for an understanding of the undertaking's activity and its impact on environmental, social and employee matters, human rights, anti-corruption and bribery. Such a report should include a description of the business model, description of policies relating to the matters above and the outcome of those policies, the principle risks in relation to those matters and any relevant non-financial key performance indicators. The NFRD also requires the inclusion of information relating to the undertaking's diversity policy or, in the absence of one, an explanatory statement.

Corporate Sustainability Due Diligence Directive (CSDDD)

The Commission adopted a proposal for the CSDDD in February 2022 that would require in-scope companies to identify and, where necessary, prevent, end or

mitigate their activities' adverse impacts on human rights and the environment. The proposal includes requirements to establish and maintain a complaints procedure, to monitor the effectiveness of due diligence policy and measures and to publicly communicate on due diligence. The proposal also introduces the opportunity for victims of harms committed by in-scope companies, their subsidiaries, contractors and suppliers, either at home or abroad, to take legal action relating to any due diligence failures before EU courts. The directive is expected to come into force during the course of 2023.

The CSDDD will first apply to all EU companies with at least 500 employees and EUR 150 million in net worldwide turnover as measured at the company level (Group 1 companies), which, in addition to the above, are required to adopt plans to ensure their business strategies are compatible with the goal of limiting global warming to 1.5°C in accordance with the Paris Agreement. Other EU limited liability companies that operate in high-impact sectors, such as textiles, agriculture and mineral extraction, which have at least 250 employees and net worldwide turnover of EUR 40 million (so-called Group 2 companies) must comply two years after the Directive applies to Group 1 companies. The rules will also apply to any non-EU companies active within the EU who meet the turnover thresholds in respect of their turnover generated within the EU.

3. What other laws/regulations in the EU touch on ESG themes?

The Conflict Minerals Regulation (Regulation 2017/821) requires EU companies to ensure they import ores and concentrates containing tin, tantalum, tungsten or gold from responsible and conflict-free sources and comply with certain supply chain due diligence obligations.

The Commission has also proposed a regulation on deforestation-free products, which would apply to all companies, irrespective of their legal form or size, placing soya, beef, palm oil, wood, cocoa, coffee products or any product derived therefrom on the EU market, or exporting them from it (COM(2021) 706 final). Under the proposal, no in-scope commodities would be allowed to enter or exit the EU market if they were produced on land either deforested or degraded after 31 December 2020. This regulation is expected to come into force in 2023.

The Directive on preventing and combating trafficking in human beings and protecting its victims constitutes a legal framework designed to fight all forms of exploitation in the EU by natural and legal persons, including sexual exploitation, begging, slavery, servitude, the exploitation of criminal activities and the removal of organs (Directive 2011/36/EU). The directive requires Member States to ensure that all legal persons are held liable for offenses committed for their benefit by any person who has a leading position within the legal person. It provides for sanctions to be raised on a legal person held liable, including exclusion from any entitlement to public benefits or aid and disqualification from the practice of commercial activities.

The European Parliament in September 2022 adopted a directive governing the adequacy of minimum wages for EU workers (COM(2020) 682 final), which

currently range widely from EUR 332 per month in Bulgaria to EUR 2,257 in Luxembourg (pre-tax). The directive does not set a fixed minimum wage but considers:

- the adequacy of minimum wages;
- the promotion of collective bargaining on wage setting; and
- effective access to minimum wage protection.

Member States would be required to monitor the adequacy of minimum wages and report to the Commission on an annual basis. The European Council formally adopted the directive in October 2022, after which Member States will have two years to implement it in national law.

EU antitrust law and policy is also becoming increasingly intertwined with considerations relating to ESG. In November 2021, the Commission published a communication in which it acknowledged that EU competition policy can contribute to the green transition by enabling companies to cooperate in the joint pursuit of genuinely green initiatives (COM(2021) 713 final). In making a competition assessment, consumer preferences for sustainable products, services and technologies should be taken into account whenever appropriate. By way of example, the Commission noted that restrictive agreements under Article 101(1) TFEU might be exempted should the sustainability-linked benefits they bring to consumers outweigh their harm. Draft revised rules on horizontal cooperation agreements between companies were published by the Commission on 1 March 2022 and aim to include a new chapter addressing the assessment of agreements pursuing sustainability objectives, including those that set sustainability standards.

In addition, recent Commission guidelines on state aid for climate, environmental protection and energy, applicable from January 2022, have aligned state aid rules with the objectives and targets of the Green Deal.

4. What, if any, litigation or enforcement activity has the EU seen related to ESG?

Enforcement of the EU's ESG frameworks, as provided for through Regulations and Directives, is left to the national governments of member states (Article 299 TFEU). Please see country-specific chapters.

5. What are the major non-law/regulatory drivers of ESG trends and developments in the EU?

Soft non-binding laws

The EU supports various UN instruments that impact businesses, including the UN Guiding Principles on Business and Human Rights, the UN's 2030 Agenda for Sustainable Development and the Sustainable Development Goals.

Stakeholders

For many stakeholders, greenwashing has become a particular concern. The European Securities and Markets Authority (ESMA) has made tackling the issue a priority in its 2022-2024 Sustainable Finance Roadmap, which includes actions to

assess greenwashing market practices, conduct case discussions on greenwashing amongst national competent authorities (NCAs) and work to develop a common understanding of NCAs' supervisory role.

In March 2022, the Commission also proposed amendments to the Unfair Commercial Practices Directive (UCPD) to address the issue of greenwashing, which include:

- adding the environmental or social impact of products to the list of characteristics about which a trader cannot mislead consumers;
- establishing the making of claims about the future environmental performance of a product without clear, objective and verifiable commitments and targets nor an effective monitoring system as a practice considered misleading; and
- including the making of generic and vague environmental claims where actual performance cannot be demonstrated in the “black list” of prohibited unfair commercial practices.

These amendments are expected to come into force in late 2023.

National Contact Points (NCPs)

Please see country-specific chapters.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

Reporting and corporate disclosure make up the focus of much of the legislation outlined in Question 2; however, the EU's ESG regulatory framework is not solely outcome-oriented. The SFDR's regulatory technical standards, for example, specify the content and methodologies in the preparation and presentation of information required under the regulation, thus prescribing the process by which in-scope firms must measure their outputs.

Other EU Directives are also process-oriented, such as the CSDDD, which provides a framework for the assessment of actual and potential adverse impacts of an undertaking's activities on human rights and the environment. See, also, the regulations and directives outlined at Question 3 above.

Reporting

Taken together, the full gamut of ESG regulations require companies to disclose across a broad range of formats. Fund managers falling subject to the SFDR must make certain entity-level disclosures in fund prospectus documentation and on their websites. Product-level disclosures are required again in fund prospectuses and in annual reports.

Non-financial reporting required of firms falling within the scope of the NFRD and proposed CSRD should be contained in annual management reports, while due diligence policies envisaged under the CSDDD must be updated by in-scope firms on an annual basis.

Reporting requirements in the EU also reflect the notion of double materiality, first coined in the NFRD, which requires a company to disclose ESG information necessary to understand the impact of its activities. While climate-related

information should be reported where necessary to understand the inward development, performance and position of the company, it must also be reported where necessary to understand the external impact of the company's activities on broader society and the environment. In this way, the materiality perspective of the NFRD covers both financial materiality and social and environmental materiality, unlike other sustainability reporting frameworks, such as the Taskforce on Climate-related Financial Disclosures, whose perspective is restricted to that of financial materiality only.

7. Which sectors are most impacted by ESG in the EU? How significant is ESG investment in the EU?

Private equity/hedge funds/asset managers

Fund managers are heavily impacted by the requirements imposed under the SFDR and, as outlined above, with the regulation requiring not only EU financial market participants and financial advisers to comply with broad sustainability-related disclosures, but also all non-EU firms marketing in the bloc. In ensuring compliance, fund managers must update marketing materials, including public websites, and source reliable and credible ESG data to form the basis of those disclosures.

Banks

European banks are coming under increasingly strict rules in relation to ESG reporting. In January 2022, the European Banking Authority published its final draft implementing technical standards on Pillar 3 disclosures in relation to ESG risks. Under the new rules, banks headquartered in the EU will be required to report on their exposure to carbon-related assets and assets subject to climate change-related risks, such as floods and fires. They must also disclose the extent to which their financing activities are aligned with the EU Taxonomy, expressed through both the Green Asset Ratio and the Banking Book Taxonomy Alignment Ratio.

European insurers are now also subject to stricter ESG-related requirements. Changes to Solvency II (Directive 2009/138/EC) effective from August 2022, for example, have seen the prudent person principle amended to include mandatory consideration by European (re)insurers of sustainability risks, and the sustainability preferences of their customers, in the investment process.

Small and medium-sized enterprises (SMEs)

In broadening the scope of the NFRD, the CSRD extends reporting requirements to all listed EU companies, including SMEs, with an opt-out available during a transition period running until 2028. Under the tiered application timeline, SMEs will be required to report from January 2026 under a proportionate set of ESRs.

On the EU's proposals for new due diligence requirements, while the CSDDD does not directly include SMEs within its scope, those who wish to do business with larger in-scope enterprises will be heavily impacted, as the directive extends to the operations of entities with which qualifying companies have established business relationships.

Fashion

Of particular relevance to the fashion industry is the Commission's Circular Economy Action Plan. As part of that plan, the Commission adopted a package of measures in March 2022 including an EU strategy for sustainable and circular textiles, aimed at ensuring that by 2030, textile products within the EU market are long-lived and recyclable, free from hazardous substances and produced with respect to social rights and the environment. Measures forming part of the strategy include:

- the introduction of mandatory eco-design requirements through a proposed Ecodesign for Sustainable Products Regulation;
- measures to prevent the destruction of unsold or returned goods; and
- measures aimed at tackling microplastics pollution.

As currently drafted, the CSDDD is also set to impact the fashion industry, with a new focus on shoring up environmental and human rights due diligence throughout the supply chain.

Greenwashing in the fashion industry is also being targeted by proposed amendments to the UCPD, as outlined above.

Automobile industry

In June 2022, the European Parliament voted to end the sale of vehicles with combustion engines in Europe by 2035. The European Parliament approved the new rules in February 2023, and the final text is now before the European Council. The legislation is a key part of the Fit for 55 package. It will likely translate into ESG regulation in relation to investment in automobile companies.

In a similar vein, the Commission is due to present a Greening of Freight Package, aiming to significantly increase energy efficiency in the sector, and consider a legislative initiative to increase the share of zero-emission vehicles in public and corporate car fleets above a certain size. The EU Save Energy Communication also includes many recommendations to cities, regions and national authorities that can effectively contribute to the substitution of fossil fuels in the transport sector.

Energy industry

The EU External Energy Strategy, adopted in May 2022, aims to facilitate energy diversification and build long-term partnerships with suppliers, including cooperation on hydrogen or other green technologies. The Commission proposes to increase the 2030 target for renewables from 40% to 45% under the Fit for 55 package. This increased target sets the framework for other initiatives.

For example, the EU aims to introduce a dedicated EU Solar Strategy to double solar photovoltaic capacity by 2025 and install 600GW by 2030. To achieve this, they aim to introduce a Solar Rooftop Initiative with a phased-in legal obligation to install solar panels on new public and commercial buildings and new residential buildings.

The EU has also set a target of 10 million tons of domestic renewable hydrogen production and 10 million tons of imports by 2030 to replace natural gas, coal and oil in hard-to-decarbonise industries and transport sectors. The Commission is also publishing two Delegated Acts on the definition and production of renewable hydrogen to ensure that production leads to net decarbonisation.

To encourage investment, the EU is also planning a Commission Recommendation to tackle slow and complex permitting for major renewable projects, and a targeted amendment to the Renewable Energy Directive to recognise renewable energy as an overriding public interest.

8. What are the trends in the EU regarding ESG governance?

Other than the CSDDD (see Question 2), there is no single EU governance law. Please see country-specific chapters for national legislative developments in governance standards.

9. To what extent are ESG ratings or ESG benchmarks relied upon in the EU?

ESG rating agencies

As sustainable investment has continued to become more integrated into the financial ecosystem, investors have increasingly come to rely on ESG rating agencies to provide data points that allow a comparison of companies' ESG credentials.

Clear evidence of the importance of ESG ratings in the European market can be seen in the various initiatives made by both the Commission and other EU authorities to address the regulation of ESG ratings and their providers. As part of the Commission's 2021 consultation on its renewed sustainable finance strategy, stakeholders were canvassed for their views on the quality and relevance of ESG ratings to their investment decisions, the degree of concentration in the market and the need for regulation and action at the EU level. In alluding to the importance of ratings and their providers, they highlighted that improved comparability and an increased reliability on ESG ratings would enhance the efficiency of the market for sustainable finance and facilitate progress under the Green Deal.

The Commission went on to undertake a targeted consultation on ESG ratings and sustainability factors in credit ratings that will directly feed into an impact assessment evaluating the impacts, costs and options of a possible EU intervention in the ratings space. In parallel, a complementary call to evidence was issued by ESMA in February 2022, aimed at mapping the ecosystem of rating providers operating within the EU and assessing the possible costs of supervision.

Responses from the combined consultations will potentially form the basis of a new policy initiative to be proposed by the Commission and designed to foster the reliability, trust and comparability of ESG ratings in early 2023.

ESG benchmarks

In relation to benchmarks, the EU has adopted the Low Carbon Benchmark Regulation, which introduced EU climate transition benchmarks and EU Paris-aligned benchmarks and seeks to ensure that low-carbon benchmarks comply with a standard methodology to provide a degree of uniformity and prevent greenwashing (Regulation (EU) 2019/2089). In July 2020, the EU Commission adopted rules setting out minimum technical requirements for the EU climate transition benchmark label. These include requirements that the sectors to

which the benchmark is allocated reduce their carbon emissions year on year and exclude assets that significantly harm ESG objectives.

While there is currently no EU benchmark encompassing all three ESG pillars, the Commission has announced the commission of a study to inform the possible features of a new EU ESG benchmark label.

10. What is the role of the private markets versus public markets in driving ESG developments in the EU?

For details of the role of companies and government-owned organisations within the EU, please see country-specific chapters.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

Access to reliable data, made more challenging by a general lack of standardisation and methodological transparency, has proved difficult for many. Requirements under the EU's ESG regulations to aggregate data, in particular non-financial data, across complex supply chains and varied portfolio companies, have proven particularly challenging.

Varying timelines for the implementation of relevant regulations have also proved burdensome, with the EU's legislative mechanics at times seeming reluctant to move. Level 2 disclosures under the SFDR, for example, were pushed back twice, eventually occurring in January 2023. Similarly, successive delays in the publication of the draft CSDDD were met with a joint statement from over 100 companies, investors, business associations and initiatives criticising these delays.

12. What information sources are most relevant for ESG considerations in the EU?

In holding responsibility for proposing legislation to the European Parliament and Council, the Commission is the primary source of information relating to ESG regulation in the EU.

13. Has the EU developed a Taxonomy related to ESG?

Yes. An outline of the EU's Taxonomy Regulation is provided at Question 2 above.

14. What does the future hold for ESG in the EU?

In the short term, the following key developments are expected over the coming years:

- The final Level 2 Regulatory Technical Standards supplementing the SFDR and including details as to the implementation of disclosures under the SFDR and Taxonomy Regulation at entity and product level are set to apply from 1 January 2023. They include five annexes with templates for principal adverse impact statements, and pre-contractual disclosure and periodic reports for Article 8 and Article 9 products.
- The Complementary Climate Delegated Act is also set to apply from 1 January 2023 and will include specific nuclear and gas energy activities in the list of economic activities covered by the EU Taxonomy.
- Preparations to meet disclosure requirements under the CSRD will begin in earnest, as regulation will become applicable initially to companies already in scope of the NFRD in 2024 (for reporting in 2025) in 2025 for all large companies (for reporting in 2026) and in 2026 for all listed SMEs (for reporting in 2027). The first set of ESRS are due for adoption by the Commission by 30 June 2023 and the second by 30 June 2024.
- Following its proposal by the Commission in July 2021, the EU Green Bond Standard (the EUGBS) is in its final negotiation phase and is expected to be released in the final version by the end of 2022, with the legislative proposal set to enter into application in 2023 or 2024. As proposed, the EUGBS would require bonds' use of proceeds to be Taxonomy-aligned, and also certain pre- and post-issuance disclosure to be reviewed by an ESMA-registered third party.
- The CSDDD is set to pass through the European Parliament and Council for approval, and its obligations are expected to apply from 2025.
- Although the timeline for its development is currently unclear, the Commission is expected to consider the establishment of a social taxonomy, likely following the end of its current mandate in 2024. This is particularly relevant in light of the publication in February 2022 by the Platform on Sustainable Finance of its final report on the social taxonomy, which suggested a structure consisting of three objectives:
 - decent work across the value chain;
 - adequate living standards and wellbeing for end-users; and
 - inclusive and sustainable communities and societies.

Looking towards the medium and long term, the EU remains set on its strategy, founded under the Green Deal, to make Europe the first climate-neutral continent by 2050. As part of this journey, the Commission has proposed in its 2030 Climate Target Plan to cut greenhouse gas emissions by at least 55% below 1990 levels by 2030, while continuing to stimulate the creation of green jobs and grow the economy. Long term, the full range of Sustainable Development Goals will filter into the substantive requirements of EU legislation as it continues to develop.

AUTHOR BIOGRAPHIES



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Patricia Volhard is a co-leader of Debevoise & Plimpton’s ESG practice and a member of the firm’s European Corporate and Investment Management Groups. Her practice focuses on advising banks, insurance companies and private fund managers on a range of European regulatory issues including on the new European ESG regulatory and disclosure requirements. Ms. Volhard is one of Europe’s leading regulatory lawyers and has played a prominent role in the ongoing development of private funds regulation and SFDR, in part through involvement in Invest Europe (formerly the European Private Equity & Venture Capital Association).



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FINLAND

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This chapter forms part of:

ENVIRONMENTAL, SOCIAL & GOVERNANCE
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1. How is “ESG” in Finland defined in a corporate/commercial context, and what are its major elements?

There is not one exhaustive definition of the term “ESG” under Finnish law. However, simply put, ESG refers to environmental, social, and governance aspects of sustainability, and in Finland, ESG is generally defined as corporate responsibility.

The Consumers’ Union of Finland, for example, defines corporate social responsibility as advancing sustainable development in companies, which includes, *inter alia*, that the company’s operations are reliable, economical, socially acceptable, and respectful towards the environment. Furthermore, socially responsible businesses respect human rights, evaluate their environmental impact, report on, and are open about, their operations. These principles are also applied to companies’ subcontractors and cooperation partners.

Although corporate responsibility in Finland is not a new phenomenon as such, Finnish companies’ ESG-related strategies and core operations are still developing and going through a turning point. Currently, many companies in Finland are evaluating the new interfaces and requirements of corporate responsibility and how to better incorporate ESG into their businesses. At the same time, corporate responsibility in Finland is becoming more regulated.

From a company law perspective, the purpose of a company is to generate profit to its shareholders, unless otherwise provided in the company’s articles of association (the Companies Act 624/2006). While ESG considerations are not explicitly mentioned as part of the purpose of a company under the Companies Act, the related preparatory works (Government Bill 109/2005) indicate that the generation of profit in the long term and the increase of the value of the company’s shares often require companies to operate in a socially acceptable way, even when not required to do so by mandatory law.

2. What, if any, are the major laws/regulations in Finland specifically related to ESG?

National legislative initiative on corporate responsibility

Even though there are several laws in Finland relating to various ESG themes, there is currently no specific legislation or regulation in Finland regarding corporate responsibility. The Finnish Government has, however, been considering enacting such law. The aim of the new legislation would have been to lay down provisions on companies’ due diligence obligations with regard to any adverse effects on human rights and the environment in their business operations. In this respect, in March 2022, the Finnish Ministry of Economic Affairs and Employment published a memorandum investigating the potential due diligence obligations that could apply to Finnish companies. The memorandum assessed in more detail the legislative options for meeting the due diligence obligations, the effect of the obligations on human rights, the environment, and companies, as well as the conditions for implementing the legislation. However, the memorandum did not include concrete regulatory proposals on, for example, the scope of companies that would be subject to the legislation. Instead, it presented alternative legislative solutions, such as different options for the scope of the obligation.

At the moment, it is expected that the national legislative initiative on corporate responsibility will not progress while the European Union's proposal for a directive on corporate sustainability due diligence is simultaneously being prepared.

In terms of ESG reporting, listed companies, credit institutions, and insurance companies that employ more than 500 employees on average are, pursuant to the Accounting Act (1336/1997), required to prepare a statement of non-financial information. The statement must include information regarding how the reporting entity handles:

- environmental matters;
- social and employee-related matters;
- respect for human rights; and
- anti-corruption and bribery matters.

The statement relates to the national implementation of the EU Directive on Non-Financial Reporting (2014/95/EU) and is expected to be amended in line with the adoption and national implementation of the EU Directive on Corporate Sustainability Reporting (CSRD).

Financial and insurance markets

In the context of financial and insurance markets, Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment (the Taxonomy Regulation), which aims to create uniform criteria for sustainable investments, applies to certain issuers and financial market participants. In addition, entities such as asset managers, investment firms, insurance companies, and credit institutions are also subject to Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector (the Sustainable Finance Disclosure Regulation) and related regulations and guidelines. The ESG amendments in the EU Directive on Markets in Financial Instruments (2014/65/EU) (MiFID II) regarding sustainability preferences apply to banks and investment firms that manufacture and distribute financial products. Moreover, from 22 November 2022, sustainability objectives and factors have to be integrated into financial product governance. The Finnish Financial Supervisory Authority (FIN-FSA) supervises financial market participants' and issuers' compliance with the Taxonomy Regulation, the Sustainable Finance Disclosure Regulation, and the MiFID II ESG amendments, and has also issued some local regulatory guidance on these issues. In terms of financial and insurance market supervision, climate change-related risks and effects on the financial sector are one of the FIN-FSA's strategic priorities, and the regulator has also expressed the aim to place an emphasis on the supervision of responsible investments reporting in the future.

3. What other laws/regulations in Finland touch on ESG themes?

Environmental

The most important piece of environmental legislation is the Environmental Protection Act (527/2014), pursuant to which companies must organise their operations in such a way that environmental pollution can be prevented in advance, and if it cannot be fully prevented, it must be limited to the lowest level possible.

Other major laws regarding environmental needs are, for example, the Nature Conservation Act (1096/1996), the Act on Environmental Impact Assessment Procedure (468/1994), the Waste Act (646/2011), the Chemicals Act (599/2013), the Forest Act (1093/1996), the Water Act (587/2011), and the Mining Act (621/2011). Additionally, the Finnish Land Use and Building Act (132/1999) is undergoing a reform process focusing on improving the effectiveness of the legislation towards climate change mitigation through, *inter alia*, proposing more extensive requirements for reducing the climate effect of buildings.

The Finnish Government supports sustainable industries by means of several regulations, such as the Act on Production Subsidy for Electricity Produced from Renewable Energy Sources (1396/2010) and the Government Decree on Granting Aid to Businesses for the Promotion of the Circular Economy and Sustainable Green Growth (1197/2020). The new Climate Change Act (423/2022), which entered into force on 1 July 2022, makes it possible to initiate legal proceedings against the Finnish Government on the basis that the Government's climate plans are deemed insufficient. Furthermore, the Act sets new climate targets and lays down provisions on the national climate change policy plans.

Social

There are a number of laws related to the social component of ESG. The most essential piece of this type of legislation is perhaps the Occupational Safety and Health Act (738/2002). The aim of this act is to improve the working environment and working conditions to protect and maintain employees' ability to work, and to prevent occupational accidents, diseases and other work-related health risks. In addition, the Non-Discrimination Act (1325/2014), the Act on Equality between Women and Men (609/1986), and the Consumer Safety Act (920/2011) are other significant examples of Finnish laws related to social issues.

Governance

There are also a number of regulations, often based on EU directives, addressing corporate governance issues.

Such regulations include, for example, the Accounting Act (1336/1997) (see also Question 6 below), which relates to sustainability reporting. Also, pursuant to the Securities Market Act (746/2012), listed companies must prepare a corporate governance statement to be either included in the issuer's board report or issued as a separate statement. Publication of the corporate governance statement increases transparency relating to good corporate governance practices. As a result of the national implementation of the EU Directive on Non-Financial Reporting, the corporate governance statement must include, among other things, a description of the principles concerning the diversity of the board of directors (including factors such as age, gender, and occupational and educational background). Other legislation concerning the "G" aspect of ESG includes, for example, the Act on Preventing Money Laundering and Terrorist Financing (444/2017), which aims to prevent money laundering and terrorist financing, promote their detection and investigation, and reinforce the tracing and recovery of the proceeds of crime.

Antitrust laws and sustainability

With regard to the relationship between antitrust laws and sustainability issues, the Finnish Competition and Consumer Authority (FCCA) has yet to issue any further guidance or decisions. The FCCA is expected to carefully follow the European Commission's approach to sustainability arguments in competition law analysis. However, the FCCA's final approach remains to be seen.

Financial and insurance markets

Apart from the Sustainable Finance Disclosure Regulation, the Taxonomy Regulation, and MiFID ESG amendments, the financial and insurance sector is generally not subject to any national ESG legislation. However, for example, certain Finnish insurers are required by law to invest pension funds profitably and securely, which can be interpreted to mean, among other things, also investing in environmentally sustainable targets. In addition, entities subject to the Act on Supplementary Pension Funds and Supplementary Pension Foundations (947/2021) are obliged to take environmental, social, and governance factors into account in their operations. Social themes, in turn, can be seen to be present in, for example, a currently pending legislative proposal that aims to restrain the indebtedness of Finnish households.

4. What, if any, litigation or enforcement activity has Finland seen related to ESG?

The first climate change case has been filed by Greenpeace against the Finnish government on an administrative law question in relation to the government's climate report on 28 November 2022. Otherwise there is currently no public litigation or enforcement activity relating specifically to ESG in Finland.

With respect to the prevention of greenwashing, the Finnish Consumer Ombudsman has issued guidelines on marketing statements that relate to the environmental effects of a product (1992, revised in 2001 and 2019).

5. What are the major non-law/regulatory drivers of ESG trends and developments in Finland?

Soft non-binding laws

Many larger Finnish companies have publicly stated their commitment to the UN Sustainable Development Goals or other non-binding international frameworks and seek to implement such goals in their strategy, policies, and procedures.

Several organisations, such as asset managers and private equity fund managers, have voluntarily committed to certain soft law principles, such as the United Nations' Principles for Responsible Investing (UN PRI), and many investors require that, for instance, fund managers take these principles into account in their operations.

Stakeholders

The Finnish Government, as well as institutional and other investors in listed companies, are some of the key stakeholders in engaging in ESG-related matters and promoting ESG aspects on companies' agenda. Pursuant to the Programme

of the Finnish Prime Minister Sanna Marin's Government, dated 10 December 2019, the Finnish Government aims to transform Finland into a socially, economically, and ecologically sustainable society by 2030. Also, pursuant to the Government resolution on the state ownership policy, dated 8 April 2020, all state-owned companies must base their operations on corporate social responsibility. In their decision-making, companies must take into account not only economic factors, but also the social, regional, and environmental impact of their activities.

Even though institutional investors are not subject to legislation imposing ESG-related requirements on their investments, some have implemented a responsible investment strategy or policy and committed to different initiatives that support responsible investing, such as the UN PRI. Consequently, certain institutional investors have stated that they emphasise ESG factors in their investments and exclude from their investments companies acting in certain industries, such as tobacco or controversial weapons, or companies whose activities are in breach of international standards. After the war in Ukraine started, many companies have also ceased their businesses in Russia due to ethical reasons and public pressure. Also, several institutional investors require specific ESG reporting from fund managers, which requires the fund managers to put in place ESG-related policies and measures for promoting and following up on ESG-related questions in their portfolio.

In particular, foreign institutional investors that have invested in Finnish public companies may rely on the ESG-related recommendations given by proxy advisors, such as the Institutional Shareholder Services group of companies (ISS). For example, the latest international sustainability proxy voting guidelines, published by ISS on 17 January 2023, also concern Finland and, among other things, include recommendations to generally vote in favour of social and environmental proposals that seek to promote good corporate citizenship while enhancing long-term shareholder and stakeholder value. In addition to institutional investors, certain non-governmental organisations are also active in promoting ESG targets, and there have been examples of NGOs proposing to include ESG-related targets in listed companies' articles of association.

Also, based on a study issued by Finance Finland in 2022, interest in green and sustainability-linked financing (e.g., loans and bonds) has grown generally in the market, and Finnish retail investors are increasingly interested in the sustainability of their investments and take, for example, possible effects on the climate into account when making investment decisions. Although there is interest in responsible investing, many investors find it difficult to assess the climate impact of their investments and companies in the financial sector work hard to make the sustainability features of investment products easier for retail investors to understand.

National Contact Points (NCPs)

The Committee on Corporate Social Responsibility of the Ministry of Economic Affairs and Employment acts as the Finnish National Contact Point for the effective implementation of the OECD Guidelines for Multinational Enterprises together with the Ministry of Economic Affairs and Employment.

The Ministry is responsible for the corporate social responsibility in the Finnish Government. Furthermore, the Committee functions in pursuit of a stronger national and international social responsibility policy, and economically, socially, and ecologically responsible operation and production methods among enterprises and other organisations.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

The requirements included in the Accounting Act relate to corporate disclosure concerning ESG aspects by means of the publication of a statement of non-financial information. In the statement, companies must describe their operating model and the principles that the company applies in managing its environmental matters, social and employee-related matters, human rights-related matters, and anti-corruption and anti-bribery matters, as well as the outcome of those principles. In relation to those, the company must also disclose the principal risks that are relevant considering the scope and extent of the company's operations, business relationships, products and services, and how the company manages those risks. In addition, the company must also disclose the non-financial key performance indicators that are relevant to its business. The statement of non-financial information must be included in the company's board report or issued as a separate statement and published annually for each financial period.

In the reporting, many large and listed companies use the international Global Reporting Initiative (GRI) Standards.

In the financial and insurance sector, the disclosure obligations consist of both outcome-based disclosures, such as the TCFD-based reporting framework established by Finance Finland, and processes for measuring outputs, for example, the forthcoming regulatory technical standards under the Sustainable Finance Disclosure Regulation.

7. Which sectors are most impacted by ESG in Finland? How significant is ESG investment in Finland?

Private equity

Private equity fund managers are impacted by ESG through the Sustainable Finance Disclosure Regulation and the Taxonomy Regulation, which require these actors to consider and disclose ESG-related matters in their operations and when marketing their products to fund investors. The Finnish Venture Capital Association has also taken an active role in promoting awareness and measures to be taken in connection with said regulation within the private equity field in Finland. Fund managers also see an increased interest from their investors in receiving information and reporting in relation to ESG-related measures, events and policies of the funds and their underlying portfolio companies. ESG due diligence is also becoming an increasingly important element of the investment processes of private equity fund managers.

Hedge funds/asset managers

Similarly to private equity fund managers, hedge fund managers and asset managers are also impacted by ESG in Finland through the Sustainable Finance Disclosure Regulation and the Taxonomy Regulation. Several asset managers are emphasising ESG in their investment operations, for example, through employing personnel focusing on ESG analysis in relation to the investment activities and by requesting their investment targets to report certain ESG-related information, for example, in connection with the due diligence process. Our understanding is that asset managers are integrating ESG in their operations more actively as a result of both the general trends of focusing on ESG and increased interest from their clients.

Banks

In addition to being subject to the Sustainable Finance Disclosure Regulation and the Taxonomy Regulation, banks are placing more and more emphasis on considering ESG-related risks in their lending operations due to, among other things, the FIN-FSA's requirement for the entities supervised by it to consider the risks and effects deriving from climate change in their operations. Banks are also increasingly providing financing specifically for sustainable purposes: for example, certain banks provide corporate loans and consumer loans that are labelled as 'green' due to being used for financing acquisitions, investments, or projects with an environmentally friendly impact. Furthermore, sustainability-linked financing products (such as loans and bonds) are increasingly offered by banks.

8. What are the trends in Finland regarding ESG governance?

ESG-related considerations are subject to increasing attention, especially among listed companies that are already subject to ESG-related reporting requirements and public scrutiny. ESG matters are common on the agendas of the boards of directors of listed companies and usually considered by the entire board instead of specially appointed committees. The implementation of the contemplated EU Directive on Corporate Sustainability Due Diligence will likely further increase the duties of boards of directors and the need to discuss and monitor the relevant ESG matters by companies' boards of directors. We have also seen a significant increase in ESG-specific roles in listed companies and the financial services sector, as companies aim to prepare for the demands of the future regulations and challenges and opportunities relating to their operating environment.

9. To what extent are ESG ratings or ESG benchmarks relied upon in Finland?

ESG rating agencies

ESG ratings are commonly used by institutional investors and fund managers as part of investment decision-making and assessing the sustainability of investments. Certain Finnish companies also utilise ESG ratings in describing

the ESG characteristics of their business and operations to their investors. Sustainalytics, MSCI, and ISS ESG are commonly used ESG rating providers in Finland. Certain financial market actors have also provided their retail investor customers with access to ESG rating data.

10. What is the role of the private markets versus public markets in driving ESG developments in Finland?

Private companies

As one example of private company-related developments in ESG reporting, the Nordic Accountant Federation (NAF), consisting of three accounting organizations in Finland, Sweden, and Norway, issued its own reporting standard in 2021, the Nordic Sustainability Reporting Standard (NSRS), which is targeted towards small and medium enterprises (SMEs) in the Nordic region and aims to support SMEs in their sustainability reporting practices.

Public companies

Many public companies have emphasised ESG considerations in their operations and seek to take ESG-related issues and risks into account in their risk mapping and risk mitigation, transactional due diligence, and commercial decision-making, in preparation for the contemplated EU Directive on Corporate Sustainability Due Diligence. In addition, many large companies regularly publish sustainability reports and, as mentioned earlier in Questions 2 and 6, certain entities are required by law to report on certain ESG-related topics. It can also be expected that public companies will want to align with ESG demands from institutional and other shareholders referred to above in the Stakeholders section of Question 5.

Nasdaq stock exchanges in the Nordic countries, including Finland, are also promoting a Green Equity Designation to listed companies. The designation would be available for companies that have over 50% of their turnover derived from activities considered green and continue to invest a significant share in green activities. Obtaining the designation would require concluding an application process with an assessment by an approved reviewer, which are currently CICERO Shades of Green and Moody's ESG Solutions.

Government-owned organizations

As mentioned above in Question 5, pursuant to the Government resolution on the state ownership policy, dated 8 April 2020, all state-owned companies must base their operations on corporate social responsibility and take into account in their decision-making not only the economic factors, but also the social, regional, and environmental impact of their activities. In addition, in summer 2022, the Finnish Government proposed amendments to the Act on Public Procurement and Concession Contract, with the aim to increase the consideration of environmental aspects and corporate responsibility in public procurement. For example, serious environmental offences would be considered grounds for exclusion from procurement for candidates, tenderers, and subcontractors.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

In the financial and insurance sector, the major challenges can be seen to relate to ensuring comparability between ESG data generated under different frameworks and by different data providers. This imposes challenges in assessing the ESG impacts of investments. For example, comparing different sustainability-linked and green financing products may be challenging when the company-specific green financing frameworks include different parameters to be monitored.

For asset managers and investors, some challenges are also posed by differing ESG reporting standards and formats, which makes comparability between target companies and funds more difficult. On the other hand, institutional investors also impose varying requirements in respect of ESG reporting, which might be deemed burdensome, in particular by fund managers.

12. What information sources are most relevant for ESG considerations in Finland?

The Ministry of Economic Affairs and Employment is responsible for corporate social responsibility (CSR) issues in the Finnish Government. CSR-related issues are also dealt with by the Ministry for Foreign Affairs (external economic relations, development policy), the Prime Minister's Office (State's ownership policy, sustainable development), and the Ministry of the Environment (environmental responsibility). Ministries coordinate their efforts and discuss them with stakeholders. CSR issues are also dealt with by the Committee on CSR, which works under the Ministry of Economic Affairs and Employment.

With regard to NGOs, Finnwatch seeks to promote ecologically, socially, and economically responsible business conduct by influencing companies, economic regulation, and public discourse. In addition, the Finnish Corporate Responsibility Law Association was established in 2020. The purpose of the association is to organise events, publish writings, and promote dialogue related to social responsibility.

In the financial and insurance sector, industry associations such as the Finnish Venture Capital Association and Finance Finland provide guidance to their members in ESG and sustainability issues. Finland's Sustainable Investment Forum (Finsif) serves as a platform for sharing knowledge and facilitating the integration of sustainability factors in investment decisions. In addition, certain institutional investors also employ private measurement frameworks such as the Task Force on Climate-related Financial Disclosures and the Carbon Disclosure Project.

13. Has Finland developed a Taxonomy related to ESG?

Apart from the EU Taxonomy framework, there is no national Finnish taxonomy.

14. What does the future hold for ESG in Finland?

As mentioned above in Question 2, it is expected that the national legislative initiative on corporate responsibility will not progress while the EU proposal for the EU Directive on Corporate Sustainability Due Diligence is simultaneously being prepared. As the contemplated EU Directive would be implemented in the national legislation and, as the political pressure is growing, it is anticipated that ESG in Finland will become more regulated in the future. Despite Finnish companies' strong commitment to the respect of human rights, the monitoring systems of complying with different fields of ESG are still insufficient and will likely be enhanced.

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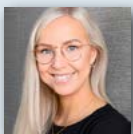
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GERMANY

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1. How is “ESG” in Germany defined in a corporate/commercial context, and what are its major elements?

Germany has not adopted a formal definition of this term.

2. What, if any, are the major laws/regulations in Germany specifically related to ESG?

Implementation of EU Law

The Sustainable Finance Disclosure Regulation (SFDR) and the Taxonomy Regulation, as EU regulations, are directly applicable in Germany. Please refer to Question 2 of the EU chapter for more information on these regulations.

The Non-Financial Reporting Directive (NFRD), the Corporate Sustainability Reporting Directive (CSRD) and the Corporate Sustainability Due Diligence Directive (CSDD), as EU directives, on the other hand, require transposition into German law in order to be legally effective in Germany (summaries of the directives can be found in Question 2 of the EU chapter). In order to implement the NFRD, the German Act to Strengthen Non-Financial Reporting by Companies in their Management Reports and Group Management Reports (CSR-Richtlinie-Umsetzungsgesetz) was ratified by the German parliament (Bundestag) on 9 March 2017. The EU proposal to revise the NFRD (the CSRD) has not yet been adopted and consequently also not yet been implemented in Germany. The draft of the CSDD has a similar aim and scope as the German Supply Chain Due Diligence Act (Lieferkettensorgfaltspflichtengesetz (Supply Chain Act)), which is already in force (see below, German Law, for more information). However, unlike the Supply Chain Act, the CSDD proposal also provides for duties that support the achievement of the EU’s climate targets. Large EU and large non-EU companies must adopt a plan to ensure that a company’s business model and strategy are consistent with the EU’s goals to transition to a sustainable economy and the EU’s actions to limit global warming to 1.5°C as defined in the Paris Agreement, and set its own emission reduction targets where necessary. As an incentive to implement the aforementioned obligations, which must also be seen in the context of climate action, the proposal stipulates that the fulfilment of these obligations is to be positively reflected in the variable remuneration of the management board. It is expected that the Supply Chain Act will be amended in order to implement the requirements set by CSDD once it has been adopted.

German Law

Supply Chain Act

The German Supply Chain Act obliges companies (with their head office, principal place of business, administrative headquarters, statutory seat or branch office in Germany) to respect human rights by implementing defined due diligence requirements. It will apply to companies with at least 3,000 employees in Germany from 2023 and to companies with at least 1,000 employees from 2024.

The Supply Chain Act contains an exhaustive catalogue of 11 internationally recognized human rights conventions. These include, in particular, the prohibition of child labour, slavery and forced labour, the disregard of occupational health

and safety, the withholding of an appropriate wage, the disregard of the right to form trade unions or employee representatives, the denial of access to food and water and the unlawful deprivation of land and livelihoods.

The law sets out the necessary preventive and remedial measures, and obliges complaint procedures and regular reporting. The core elements of the due diligence obligations include the establishment of risk management to identify, prevent or minimize the risks of human rights violations and damage to the environment. Due diligence obligations will apply to a company's own business operations, to the actions of a contractual partner and to the actions of other (indirect) suppliers. This means that a company's responsibility no longer ends at their own factory gate, but exists along their entire supply chain.

If companies fail to comply with their legal obligations, fines can be imposed. These can amount to up to EUR 8 million or up to 2% of global annual sales. The turnover-based fine framework only applies to companies with annual sales of more than EUR 400 million. In addition, if a fine is imposed above a certain minimum level, it is possible to be excluded from the award of public contracts.

First and Second Leadership Positions Act

On 11 August 2021, the German Second Leadership Positions Act (*Zweites Führungspositionengesetz* (LPA II)) entered into force. As a continuation of the First Leadership Positions Act of 2015 (LPA I), the LPA II introduced a minimum participation requirement for men and women in management boards of companies within its scope. It extends commercial reporting obligations and requires companies to disclose and justify target quotas for their board appointments.

Under the LPA I, listed companies and companies with equal co-determination were subject to a fixed gender quota of 30% for their supervisory boards and had to define a target size for male and female participation on their supervisory and management boards (so-called "flexible quota").

The LPA II does not provide for a fixed quota, but prescribes a minimum participation requirement for management boards of listed and co-determined companies of at least one woman and one man if the board consists of more than three members. One common feature with the LPA I is that appointments made in violation of this requirement are void (so-called "empty chair"). In practice, this means that only a woman can be appointed as a member of the management board if a board has more than three members, but not yet a female member. This obligation applies to new appointments from 1 August 2022. Existing mandates can be held until their scheduled end must then be filled in accordance with the requirements of the LPA II.

In addition, listed companies and companies with equal co-determination must now publicly report their target size for appointments to the management board in their annual accounts (part of the management report). The target of zero women on the board must now be justified. Failure to report or inadequate justification are subject to fines. For companies active in capital markets, sanctions can go up to either EUR 10 Million, 5% of the total annual turnover or twice the economic benefit derived from the violation, depending on which is the highest punishment.

The LPA II also creates the option for members of the management board to take a “sabbatical” in the event of maternity leave, parental leave, illness or care of a family member. This is structured as a right to revoke the appointment for a certain period, combined with a right to reappointment at the end of the period.

3. What other laws/regulations in Germany touch on ESG themes?

EU Conflict Minerals Regulation

The EU Conflict Minerals Regulation is directly applicable in Germany. Please refer to Question 3 of the EU chapter for more information on this regulation.

Act to Improve the Fight against Trafficking in Human Beings

The German Act to Improve the Fight against Trafficking in Human Beings and to Amend the Federal Central Register Act and the Eighth Book of the Social Code (Gesetz zur Verbesserung der Bekämpfung des Menschenhandels und zur Änderung des Bundeszentralregistergesetzes und des Achten Buches Sozialgesetzbuch (Act Against Human Trafficking)), which entered into force on 15 October 2016, implements the EU Directive on preventing and combating trafficking in human beings and protecting its victims. Please refer to Question 3 of the EU chapter for more information on this directive. The combating of human trafficking and the support of its victims are strongly supported by the German Federal Ministry of Justice and Consumer Protection (Bundesministerium der Justiz und für Verbraucherschutz).

In the course of the implementation of the EU directive, the criminal provisions for combating trafficking of human beings in Sections 232 to 233a of the German Criminal Code (Strafgesetzbuch) were fundamentally restructured and expanded.

The actual trafficking of human beings (Section 232 of the German Criminal Code) and the forms of exploitation that follow it (forced prostitution, forced labour and exploitation of labour and exploitation using deprivation of liberty – Sections 232a to 233a of the German Criminal Code) constitute serious criminal offenses. The fundamental reorganization and expansion of the relevant criminal provisions was intended to make them more practicable and, in particular, to improve the fight against labour exploitation.

European Shareholder Rights Directive

Following implementation of the second European Shareholder Rights Directive and the revision of the German Corporate Governance Code (Deutscher Corporate Governance Kodex), German stock corporation law stipulates that in listed companies, the supervisory board must align the management board remuneration structure with the company’s sustainable long-term development.

4. What, if any, litigation or enforcement activity has Germany seen related to ESG?

The increasing density of regulations in the environmental and social sector can give rise to additional costs, but also to fines or liability risks. In recent

years, the lawsuits filed/announced by Deutsche Umwelthilfe e.V., a German environmental, nature and consumer protection organization, against, *inter alia*, automobile manufacturers BMW and Mercedes-Benz and the oil and gas group Wintershall Dea over their CO2 emissions, have made headlines in Germany.

5. What are the major non-law/regulatory drivers of ESG trends and developments in Germany?

Soft non-binding laws

Germany supports various UN instruments that impact businesses, including:

- the UN Guiding Principles on Business and Human Rights;
- the UN's 2030 Agenda for Sustainable Development; and
- the Sustainable Development Goals.

Other soft non-binding laws include:

- The OECD Guidelines for Multinational Enterprises set out recommendations on responsible business conduct for multinational companies that operate in a global context. The Guidelines contain established principles of responsible business conduct in the areas of information policy, human rights, employment policy, environmental protection, anti-corruption, consumer interests, science and technology, competition and taxation. The Guidelines, which form part of the OECD Declaration on International Investment and Multinational Enterprises, are not legally binding, but reflect the Federal Government's expectations towards the business conduct of German enterprises that operate globally. See www.bmwk.de/Redaktion/DE/Downloads/M-O/oecd-leitsaetze-fuer-multinationale-unternehmen-neufassung-2011-englisch.pdf.
- In 2016, the German government agreed on a so-called National Action Plan on Business and Human Rights, which emphasized the responsibility of German companies to respect human rights. The Supply Chain Act, for example, serves to implement the Action Plan. The action plan in turn is based on the 2011 UN Guiding Principles on Business and Human Rights, which are intended to ensure respect for human rights in business relations.
- The German Sustainability Strategy translates the Sustainable Development Goals (SDGs) of the United Nations, the so-called "Agenda 2030", into a national strategy.
- The German Corporate Governance Code (Deutscher Corporate Governance Kodex, (GCGC)) presents essential statutory regulations for the management and supervision of German listed companies and contains, in the form of recommendations and suggestions, internationally and nationally acknowledged standards for good and responsible corporate governance. In January of 2022, the Government Commission on the German Corporate Governance Code (Regierungskommission Deutscher Corporate Governance Kodex) adopted an updated draft of the GCGC in order to account for the growing importance of ESG aspects and the expansion of reporting requirements as a result of the announced CSRD, as well as the recent amendments to the German Stock Corporation Act (AktG) by the German Financial Market Integrity Strengthening Act (Gesetz zur Stärkung der Integrität der Finanzmärkte) and

the LPA II. Pursuant to a current draft of the new GCGC, the management board shall systematically identify and assess the risks and opportunities for the company associated with social and environmental factors, as well as the environmental and social impacts of the company's activities. Information on the corporate strategy shall provide information on how to implement the economic, ecological and social objectives in a balanced manner.

- The German Federal Financial Supervisory Authority (BaFin) regularly publishes guidelines and Q&As regarding sustainability requirements. In particular, in December 2019, BaFin published its Guidance Notice on Dealing with Sustainability Risks, which BaFin considers as a compendium of non-binding procedures (good practice principles) with respect to the implementation of a proper business organisation and an appropriate risk management system in connection with sustainability risks. In contrast, BaFin put on hold its plan to introduce guidelines for sustainable funds due to the regulatory, energy and geopolitical situation and the concern that the current environment is not sufficiently stable for a permanent regulation.
- The German Sustainability Code (Nachhaltigkeitskodex) was developed in 2010 by the German Council for Sustainable Development (Rat für Nachhaltige Entwicklung (RNE)) in a dialog process with representatives of politics, the financial market, companies and civil society organizations. The German Sustainability Code provides a framework of an internationally applicable reporting standard for topics relating to sustainability pursuant to which users declare their conformity with 20 criteria and the additional non-financial performance indicators taken from the Global Reporting Initiative (GRI) and the European Federation of Financial Analysts Societies (EFFAS).

Stakeholders

Sustainability encompasses all areas of political responsibility. Due to this cross-cutting nature and the particular importance of the topic, responsibility for the German Sustainability Strategy lies with the Federal Chancellery (Bundeskanzleramt). The State Secretary's Committee for Sustainable Development (Staatssekretärsausschuss für nachhaltige Entwicklung) is the most important steering body of the government's sustainability strategy. It is also the government's highest-ranking body and is tasked with ensuring that the guiding principles of sustainability are applied. State secretaries from all federal ministries take part in its meetings, which are held up to four times a year.

The RNE advises the German government on sustainability policy. It is independent in its activities and has been appointed by the German government every three years since 2001. The RNE also carries out its own projects to advance sustainability in practice. In addition, it provides impetus for political and social dialog.

In 2004, the German government decided to establish the Parliamentary Advisory Council for Sustainable Development (Parlamentarische Beirat für nachhaltige Entwicklung). Since then, it has been newly appointed and constituted at the beginning of each legislative period and is to provide parliamentary support and recommendations for the German sustainability strategy of the federal government, the European sustainability strategy and the sustainability policy of the German government at the international level.

Deutsche Umwelthilfe e. V. (DUH), a German environmental, nature and consumer protection organization, made headlines in Germany in recent years. DUH is committed to climate protection, the preservation of biodiversity, an energy supply based on efficiency and renewable sources, resource conservation and recycling management, clean air, sustainable mobility and consumer protection. Since 2009, DUH has received grants from the U.S. Climate Works Foundation, the EU Commission and the German federal government as part of an EU-wide campaign to reduce soot emissions.

National Contact Points (NCPs)

The German Federal Ministry for Economic Affairs and Climate Action (Bundesministerium für Wirtschaft und Klimaschutz) acts as the National Contact Point for the OECD Guidelines in Germany.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

EU legislation

Reporting and corporate disclosure make up the focus of much of the EU legislation outlined in Question 2. Please refer to Question 6 of the EU chapter for more information on the EU instruments applicable in Germany.

Supply Chain Act

Under the Supply Chain Act, companies must submit an annual report to the Federal Office of Economics and Export Control (Bundesamt für Wirtschaft und Ausfuhrkontrolle) on the implementation of due diligence obligations and publish it online.

The report must provide comprehensible information on:

- whether and which human rights and environmental risks the company has identified;
- what the company has done to fulfil its due diligence obligations;
- how the company assesses the impact and effectiveness of the measures; and
- what conclusions it draws from the assessment for future action.

The report must be made publicly available online no later than four months after the end of the fiscal year and must be available for seven years. Company and business secrets must be duly protected. The reports are submitted to the Federal Office of Economics and Export Control. Work is underway on an electronic procedure to minimize the burden on companies.

First and Second Leadership Positions Act

As outlined in Question 2 above, the LLP I and the LLP II require disclosure and, in case of a zero target, justification of the targeted participation quota as part of the management report in the annual accounts.

A zero target must be justified in a clear and comprehensible manner; the justification must set out in detail the considerations on which the decision is based. The statement of reasons should take account of the exceptional nature of the zero target. Accordingly, the German government believes that the statement

of reasons must make a conscientious decision plausible to the public. As a guideline for the level of detail, the explanatory memorandum states a length of 100 to 150 words.

7. Which sectors are most impacted by ESG in Germany? How significant is ESG investment in Germany?

EU legislation

Please refer to Question 7 of the EU chapter for more information on impact of the EU instruments applicable in Germany.

Supply Chain Act and CSDD

The Supply Chain Act holds companies responsible for breaches in their supply chain, directly and indirectly (e.g., by sub-contractors), in Germany and abroad. It is difficult to imagine a sector that will not be influenced by the new diligence requirements. The “high-impact sectors” include textiles, food, agriculture, fisheries, forestry, the extraction of mineral resources, the manufacture of base metal products and other non-metallic mineral products and the wholesale of mineral raw materials, base and intermediate minerals.

First and Second Leadership Positions Act

A minimum participation requirement of one woman applies to management boards with more than three members of listed companies and companies with equal co-determination. Pursuant to information published by the competent German Federal Ministry for Family Affairs, Senior Citizens, Women and Youth (Bundesministerium für Familie, Senioren, Frauen und Jugend) in August of 2021, this law affected 66 companies in total (no indication of sector given), of which 21 currently had no women on their boards.

8. What are the trends in Germany regarding ESG governance?

Last May, the new German government presented a new strategy for sustainable financing and a tightening of the climate protection law. For example, Germany is to become climate-neutral as early as 2045 (instead of 2050), and emissions are to fall by 65% by 2030 (compared with 1990). To achieve this goal, the government has adopted 26 measures to mobilize trillions in investment for more climate protection. These include, among other things, an (EU-wide) sustainability traffic light for financial products, an extended sustainability reporting obligation and the reallocation of investment funds from the federal government to sustainable investments.

9. To what extent are ESG ratings or ESG benchmarks relied upon in Germany?

ESG rating agencies

The German government has developed a sustainability action program and provides an annual account of implementation in a monitoring report. The Federal

Statistical Office's (Statistisches Bundesamtes) indicator report, published every two years, forms the basis for the federal government to adjust its measures.

In their 2021 coalition agreement, the German ruling parties agreed to promote European minimum requirements for ESG ratings.

Please refer to Question 9 of the EU chapter for more information from a European perspective.

ESG benchmarks

Please refer to Question 9 of the EU chapter for more information on European ESG benchmarks which are relied upon in Germany.

10. What is the role of the private markets versus public markets in driving ESG developments in Germany?

Consumer demands play a major role in driving ESG developments in Germany. Recent events (the COVID-19 pandemic, floods in western Germany, historical temperature highs, the Me Too and Black Lives Matter movements, Friday for Future demonstrations, war in Ukraine) have increased awareness for social and environmental matters for the everyday consumer. The pressure on politicians and companies to implement meaningful ESG measures will likely increase further and bring additional regulations for all aspects of the economy and society.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

As in other jurisdictions, the major challenges are:

- the collection of reliable ESG data;
- the difficulties in the application of ESG laws by lack of clarification; and
- the varying timelines for the implementation of relevant ESG regulations.

12. What information sources are most relevant for ESG considerations in Germany?

With respect to EU instruments and their interpretation, the EU Commission is the primary source of information.

With respect to corporate ESG requirements and measures, the GCGC provides valuable guidance.

13. Has Germany developed a Taxonomy related to ESG?

Yes. The EU Taxonomy Regulation is directly applicable in Germany. Please refer to Question 2 of the EU chapter for an outline of the regulation.

14. What does the future hold for ESG in Germany?

It is likely that, as ESG capital flows grow, so will greenwashing. The amount of misleading information about the actual environmental, social and governance performance of companies and their products will likely increase. As a result, the importance of consistent and comparable sustainability reporting based on a single global standard for measuring and communicating ESG performance will increase. For future developments, please see Question 14 of the EU chapter, as the European Union with its Green Deal initiative is a key driver of ESG development.

AUTHOR BIOGRAPHIES



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Patricia Volhard is a co-leader of Debevoise & Plimpton's ESG practice and a member of the firm's European Corporate and Investment Management Groups. Her practice focuses on advising banks, insurance companies and private fund managers on a range of European regulatory issues including on the new European ESG regulatory and disclosure requirements. Ms. Volhard is one of Europe's leading regulatory lawyers and has played a prominent role in the ongoing development of private funds regulation and SFDR, in part through involvement in Invest Europe (formerly the European Private Equity & Venture Capital Association).



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ITALY

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1. How is “ESG” in Italy defined in a corporate/commercial context, and what are its major elements?

Italian ESG regulation is based, primarily, on European legal sources of direct or indirect application in Italy (i.e., Regulations or Directives).

However, there is also important domestic legislation. For example, Italy is the first European country to regulate a Benefit Corporation model, the “Società Benefit” (Law 208/2015). This is a legal status (and not a legal form) that can be obtained by any “traditional” company, regardless of its operating sector, provided its bylaws include the purposes of pursuing a common benefit as well as distributing profits (as well as other legal requirement).

The major characteristics of ESG in Italy are:

- The bond with the EU regulatory framework, which acts as a catalyst for domestic regulatory development.
- The focus on disclosure and risk management, with an increasing importance placed on due diligence and governance matters.
- The high regulation for financial intermediaries (hedge funds, banks, etc.), which is boosting ESG adoption amongst the corporate sector through the investment/credit value chain.
- The link with the third-sector (recently reformed through Legislative Decree 117/2017 and made of non-profit entities), which is traditionally oriented to the pursuit of general interest purposes and the inclusion of stakeholders. These themes are now expanding to the market-driven private sector (profit-making enterprises), whether on a voluntary or regulatory basis.

2. What, if any, are the major laws/regulations in Italy specifically related to ESG?

The following domestic legislation directly address ESG:

- Interministerial Decree of March 29, 2022, which defines how to prepare the biennial report regarding male and female employees in public and private companies with more than 50 employees.
- Law 162/2021, on amendments to the Code on Equal Opportunity (Legislative Decree 246/2005, as complemented by Legislative Decree 198/2006), and other provisions on equal opportunities between men and women in employment.
- Decree of the Italian Minister of Labour and Social Policy of 23 July 2019, with guidelines for the implementation of systems for assessing the social impact of the activities carried out by third-sector entities.
- Decree of the Italian Minister of Labour and Social Policy of 4 July 2019, on the adoption of guidelines for the preparation of the social report of third-sector entities.
- Legislative Decree 117/2017, Code of Third-sector Entities.
- Legislative Decree 112/2017, Revision of the discipline of Social Enterprises (as complemented by Legislative Decree 95/2018).
- Legislative Decree 254/2016 implementing Directive (EU) 2014/95 on non-financial reporting (NFRD).
- Law 208/2015, establishing the Italian Benefit Corporation (Società Benefit).

- Decree-Law 179/2012, establishing the Innovative Start-up with Social Vocation (SIAVS).

The following EU legislation, directly or indirectly, addresses ESG and directly applies in the domestic context:

- Directive (EU) 2022/2464 amending Regulation (EU) 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting (CSRD).
- Commission Delegated Regulation (EU) 2022/1288 supplementing Regulation (EU) 2019/2088 with regard to regulatory technical standards specifying the details of the content and presentation of sustainability information (RTS).
- Commission Delegated Directive (EU) 2021/1270 amending Directive 2010/43/EU as regards the sustainability risks and sustainability factors to be taken into account for Undertakings for Collective Investment in Transferable Securities (UCITS).
- Commission Delegated Directive (EU) 2021/1269 amending Delegated Directive (EU) 2017/593 as regards the integration of sustainability factors into the product governance obligations.
- Commission Delegated Regulation (EU) 2021/1257 amending Delegated Regulations (EU) 2017/2358 and (EU) 2017/2359 as regards the integration of sustainability factors, risks and preferences into the product oversight and governance requirements for insurance undertakings and insurance distributors and into the rules on conduct of business and investment advice for insurance-based investment products.
- Commission Delegated Regulation (EU) 2021/1256 amending Delegated Regulation (EU) 2015/35 as regards the integration of sustainability risks in the governance of insurance and reinsurance undertakings.
- Commission Delegated Regulation (EU) 2021/1255 amending Delegated Regulation (EU) No. 231/2013 as regards the sustainability risks and sustainability factors to be taken into account by Alternative Investment Fund Managers.
- Commission Delegated Regulation (EU) 2021/1253 amending Delegated Regulation (EU) 2017/565 as regards the integration of sustainability factors, risks and preferences into certain organisational requirements and operating conditions for investment firms.
- Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088 (EU Taxonomy).
- Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector (SFDR).
- Regulation (EU) 2017/1991 amending Regulation (EU) 345/2013 on European venture capital funds and Regulation (EU) 346/2013 on European social entrepreneurship funds.
- Regulation (EU) 2017/821 regarding supply chain due diligence obligations for importers of tin, tantalum and tungsten, their ores and gold originating from conflict-affected and high-risk areas.
- Regulation (EU) 346/2013 on European social entrepreneurship funds (EuSEF funds).

In addition, the Corporate Sustainability Due Diligence Directive (CSDD) is expected. Drafted by the EU Commission, this Directive proposal aims to establish due diligence obligations to prevent, cease or minimize potential negative impacts on the environment and human rights.

3. What other laws/regulations in Italy touch on ESG themes?

The following domestic legislation, indirectly, addresses ESG:

- Decree Law 77/2021, on the governance of the National Recovery and Resilience Plan (PNRR).
- Law 157/2019 amending the Code of Public Contracts (Legislative Decree 50/2016), providing reward criteria mechanisms for entities that measure their impact through the “external evaluation standard” of the Società Benefit.
- Legislative Decree 231/2001 with regulations on the administrative liability of legal persons, companies and associations, including those without legal personality.

Art. 47 of Decree Law 77/2021 introduces incentive requirements in public tenders, aimed at promoting youth entrepreneurship, gender equality and the hiring of young people and women. The Decree also introduces special measures on renewable sources, energy efficiency, the promotion of a circular economy and combating hydrogeological instability.

Law 157/2019 represents a key step towards greater diffusion of social and environmental impact assessments. For example, the Decree rewards companies that measure their ESG impact, since it includes impact assessment among the criteria of the National Anti-Corruption Authority (ANAC) for the determination of a company rating – a tool to compare the reputation of economic operators in public procedures. Moreover, the Decree provides that the Public Administration can award a higher score in calls for tenders if:

- the companies carry out a social impact assessment; or
- the offer concerns “goods, works or services with a lower impact on health and the environment, including goods or products from short or zero kilometer supply chains”.

Legislative Decree 231/2001 introduced a tool (the 231 model) aimed at mitigating the risk of the commission of certain crimes by some individuals in the interest or to the benefit of the legal entity. The internal control system implemented through this 231 model can also contribute, indirectly, to the pursuit of sustainability goals, at least in managing the risks of negative impacts. For example, the model can be used to prevent the commission of environmental crimes while encouraging “sustainable” conduct.

4. What, if any, litigation or enforcement activity has Italy seen related to ESG?

The only case of ESG litigation involved accusations of greenwashing and misleading advertising. On 25 November 2021, the Court of Gorizia issued a “precautionary” order against a company found guilty of promoting products with unsubstantiated “green” characteristics. The Court prohibited the company from disseminating the misleading advertising and enjoined to publish the order on the company’s website.

With respect to public enforcement, it is worth noting that:

- The Antitrust Authority (AGCM) has been entrusted with the role of supervising, preventing and sanctioning misleading green claims and greenwashing.
- In April 2022 Bank of Italy issued an initial set of expectations on the integration of climate and environmental risks into business strategy, governance, control and risk management systems and market reporting of supervised financial intermediaries, followed by a note, issued on December 2022, containing further indication.
- The National Commission for Companies and the Stock Exchange (CONSOB) has initiated a process to align the Intermediaries Regulation and the Issuers Regulation with some of the EU main legal acts on ESG.

5. What are the major non-law/regulatory drivers of ESG trends and developments in Italy?

Soft non-binding laws

Italy has ratified numerous international conventions that represent the highest non-binding ESG framework, such as the:

- Universal Declaration on Human Rights;
- United Nations Framework Convention on Climate Change;
- ILO Conventions;
- 2030 Agenda for Sustainable Development (SDGs); and
- Paris Agreement.

There are also soft laws and standards to which several Italian companies adhere to in order to align their business model to global ESG trends, such as the:

- UN Guiding Principles of Business and Human Rights (UN Guiding Principles);
- UN PRI;
- OECD Guidelines for Multinational Enterprises (OECD Guidelines); and
- UN Global Compact.

The SFDR and EU Taxonomy recall some of the above instruments, making them enforceable. For example, Art. 18 of the EU Taxonomy considers as “minimum safeguards” the alignment of a company with the OECD Guidelines and the UN Guiding Principles.

Stakeholders

ESG issues in Italy have become a trend and are constantly in the spotlight. In particular:

- Retail investors are increasingly engaging in ESG, as also highlighted at the EU level by Eurosif in a survey on the SRI industry (2018). Consistently, the EU Commission has provided for an integration of sustainability factors, risks and preferences into certain organizational requirements and operating conditions for investment firms (see Commission Delegated Regulation (EU) 2021/1253).
- Institutional investors are contributing to the spread of ESG practices with their own (dynamic and context-specific) views about what ESG factors are relevant and what constitutes “impact”. A survey conducted in May 2022 by Assofondi Pensione found that 68% of Italian pension funds have a public

commitment to adopt strategies consistent with ESG factors. This figure is up from the previous year (50%). Another survey (November 2021) by the Italian Sustainable Investment Forum (ItaSIF) made clear that exclusions and ‘best-in-class’ are the most widely used ESG strategies by pension fund investors, and revealed a growing interest in engagement and proxy voting (following the transposition of the Shareholders Rights II Directive).

- Private companies are strongly promoting ESG practices. For example, through the UN Global Compact Network Italia (UNGCN Italia), which has among its founders leading companies from various industrial sectors including ENI (oil and gas), Aeroporti di Roma (travel and leisure), Andriani (food and beverage) and Legance - Avvocati Associati (legal services). This network fosters the adoption of 10 principles relating to human rights, labour standards, environmental protection and anti-corruption among Italian companies.
- The Italian government, driven by EU policies (such as the Next Generation EU program for financing EU economic recovery through the dual ecological and digital transition), set forth the PNRR, which is structured around digitalization and innovation, ecological transition and social inclusion, with a clear ESG focus. The reforms and investments envisaged by the plan aim to promote sustainable development with positive long-term impacts for the community and the environment through specific “ESG-oriented” resource allocation criteria.

Different motivations are driving such stakeholders, for example:

- creating shared ESG standards and best practices;
- achieving the SDGs;
- ensuring a just transition; and
- countering greenwashing practices.

National Contact Points (NCPs)

National contact points of international organizations are also active in promoting ESG in Italy. Alongside the UNGCN Italia, there are, for example:

- the Italian OECD National Contact Point for Responsible Business Conduct; and
- the Social Impact Agenda for Italy (SIA), the Italian National Advisory Board (NAB) of the Global Steering Group for Impact Investments (GSG).

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

There is a primary focus within the current regulatory framework on ESG disclosure at the corporate and investment fund level. In general, it is possible to distinguish among ESG laws that aim to regulate:

- **Legal forms or statuses** of entities characterized by a business model that balances profit with the pursuit of common benefit goals (i.e., the discipline on Social Enterprises, Società Benefit, SIAVS, EuSEF funds).
- **Impact/ESG measurement and reporting**, in an attempt to disseminate and standardize these practices (i.e., the rules on the non-financial reporting or the biennial report on gender balance, as well as the RTS).

- **Other key ESG procedures** (i.e., ESG risk management, sustainability-related disclosures, integration of sustainability factors into product governance for investment firms, due diligence obligations for some importers and so on).
- **Specific hot ESG topics** (i.e., the Equal Opportunity Code).
- **General ESG framework** (i.e., the framework under the EU Taxonomy to facilitate sustainable investment).

Reporting

The SFDR provides for sustainability-related disclosure in pre-contractual documents and periodic reports, as well as on the web. Such disclosures follow the detailed provisions of the RTS.

With regard to the NFRD, non-financial statements may be contained in a specific section of the management report or in a separate report. In order to promote better usability of the information, it is possible to use the so-called “incorporation by reference technique”. Pending the drafting of specific EU reporting standards, the most widely used tool is the GRI Standard. Finally, a key aspect is the analysis of dual materiality: although not currently required by NFRD (but will be by CSRD), the main reporting standards include this aspect.

Società Benefit must draw up an annual report (based on a legal standard) on the achievement of ESG purposes and on the “impact” generated. The financial statements shall include such a report.

SIAVS must file, every year, the “social impact description document” (based on a reporting standard of the Ministry of Economic Development) with the Chamber of Commerce and publish it on their website.

Social Enterprises must file the “social report” (based on a reporting standard of the Ministry of Labour and Social Policies) with the Business Register and publish it on their website.

7. Which sectors are most impacted by ESG in Italy? How significant is ESG investment in Italy?

The consideration of ESG factors, once an option, is now an obligation for an increasing number of sectors.

As already noted, one of the most affected sectors is financial intermediaries, such as private equity firms, hedge funds, asset managers and banks (especially with respect to ESG reporting and risk management).

In addition, asset managers and companies involved in the real estate industry are increasingly adopting sustainability certifications (i.e., the Leadership in Energy and Environmental Design (LEED) and the Building Research Establishment Environmental Assessment Method (BREEAM)) and integrating ESG factors into business models.

For sectors relying heavily on supply-chains, such as fashion and automotive, ESG criteria appears to be expanding beyond the organisational and business models of single companies, stimulating suppliers, partners and institutions to adopt sustainability-oriented approaches.

8. What are the trends in Italy regarding ESG governance?

Increasingly, a widespread practice within medium to large companies is the appointment of ESG officers (such as a Chief Sustainability Officer or a Chief Impact Officer for Società Benefit). This is often coupled with the establishment of ESG committees, to advise the board on ESG issues and manage functions such as ESG measurement and reporting, as well as ESG risk management.

This appears to be an established trend, considering that – as highlighted by a 2018 study of the CSR Manager Network – 80% of listed companies already have an internal board committee with delegated responsibility for sustainability, and 15% have established a specific committee dealing exclusively with sustainability.

In addition, with respect to governing bodies, there appears to be a particular attention to gender balance and directors' remuneration, which is often linked to the achievement of ESG targets.

9. To what extent are ESG ratings or ESG benchmarks relied upon in Italy?

ESG ratings and standards are popular in Italy, as they are key tools to determine the sustainability level of investments and companies.

However, the multitude of these instruments, which follow different rules and principles, makes data comparability and interpretation difficult. Consequently, there is an increasing reliance on legal tools provided by the EU to classify economic activities as sustainable (i.e., EU Taxonomy) and to make proper disclosure (i.e., SFDR and RTS).

10. What is the role of the private markets versus public markets in driving ESG developments in Italy?

Both private and public markets are key players in achieving the transition to a sustainable economy. In particular, the EU strategy is focused on leveraging the role played by large private and public companies, requiring extensive and detailed disclosure requirements (i.e., under the SFDR, the NFRD and, looking forward, the CSRD proposed directive). More specifically – in accordance with such laws – banks, insurance companies, listed companies and financial intermediaries should report detailed sustainability-related information. As a consequence, many Italian companies are increasingly integrating ESG factors into their business strategies.

Public companies are also asked to comply with the Code of Corporate Governance for Listed Companies. Such Code requires the board to promote the so-called “sustainable success”, intended as a long-term strategy of value creation, for shareholders, that shall also take into account the interests of a company's stakeholders.

A noteworthy case study is that of Reti S.p.A., the first listed company with the legal status of “Società Benefit” and in possession of the B Corp certification. Its ESG-oriented business model has contributed to a successful placement of shares in 2020 that registered a total demand of about 1.3 times the initial offering.

Certainly, an increasing number of both public and private companies are adopting ESG policies, procedures, certifications and legal statuses, aiming to prevent and minimize the company's environmental and social risks, along with generating ESG value. Such a trend is both market- and regulatory-driven.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

Several challenges exist with respect to ESG effectiveness and integrity which ultimately facilitates greenwashing practices, for example:

- Access to ESG data: the Italian ecosystem is still strongly composed of SMEs for which the cost related to measuring non-financial data represents a barrier that affects the ESG disclosure of the entire value chain.
- Quality of non-financial data: unlike financial data, this is often not validated by audit processes, with the risk for the market to have unreliable data of a very low quality.
- Misalignment of sustainability disclosure standards: a global phenomenon, due to a lack (in some cases), of interoperability of the international organizations involved in the development of such standards.
- Measurement of "S" factors: still underdeveloped compared to "E" factors.
- Uncertainty around "G" factors: given an unclear definition of what might be good governance practices.
- Legal uncertainties: as the regulatory framework is still in its first steps, integration and interpretation by the EU and domestic authorities, is required to ensure uniformity in application.
- Economic instability: which tends to reinforce profit maximization logics at the expense of proper management and integration of ESG risks and opportunities.

A first response to these challenges comes from regulatory developments, especially at the EU level. The SFDR, the EU Taxonomy, the CSRD and the proposed CSDD directive go in this direction, addressing some of the mentioned barriers.

12. What information sources are most relevant for ESG considerations in Italy?

A key source of ESG information is national supervisory authorities, which contribute (through surveys and reports) to disseminating knowledge with respect to ESG market practices and the evolution of regulatory frameworks. Numerous indications are coming, for example, from CONSOB and the Bank of Italy, partly because of the greater prominence, for now, of the ESG phenomenon with respect to the financial intermediary sector.

In addition, academic institutions play a significant role in the promotion and evolution of ESG practices. As an example, the Polytechnic University of Milan, University of Bologna, Polytechnic University of Turin and Sapienza University of Rome have teams of researchers and lecturers focused on different

aspects of sustainability and social innovation. As a further example, TIRESIA, an international research centre promoted by the School of Management of the Polytechnic University of Milan, pursues scientific excellence in the field of social impact innovation and sustainability.

Important contributions to the ESG expansion also come from third-sector entities and important national networks, such as:

- Social Impact Agenda for Italy.
- Torino Social Impact, a network also supported by Turin's municipal administration.
- Cottino Social Impact Campus, the first campus in Europe exclusively dedicated to the culture of social impact.
- Forum per la Finanza Sostenibile, a non-profit association promoting ESG criteria in financial products.
- Assobenefit, the association for Società Benefit in Italy.

13. Has Italy developed a Taxonomy related to ESG?

The EU Taxonomy (Regulation (EU) 2020/852) directly applies in the national context and establishes an ESG framework to facilitate sustainable investment.

This legislation:

- defines the main criteria for environmentally sustainable economic activities;
- provides specific transparency obligations (in addition to those under the SFDR) to financial market participants;
- provides similar obligations for undertakings (those subject to non-financial reporting pursuant to article 19(a) or article 29(a) of Directive 2013/34/EU); and
- mandates the European Commission to extend the scope of such taxonomy beyond environmentally sustainable economic activities, covering other sustainability objectives, such as social objectives.

14. What does the future hold for ESG in Italy?

Looking forward, we can expect the following trends and developments.

In the short term:

- Initial misalignment with the RTS (entered into force the 1st of January 2023), which financial intermediaries will have to comply with regarding sustainability-related disclosures.
- Increase in the adoption of ESG safeguards and strategies by market players (although this phenomenon may be slowed by economic instability that pushes for profit maximization and short-termism), as, for example, a further proliferation of funds qualified under Art. 8 of SFDR.
- Additional focus of EU and national supervisory authorities with respect to ESG issues, through further guidance, surveys and first assessments/inspections.
- Increased concern for social issues and respect for human rights at a corporate level.

- Persistence of a misalignment with other jurisdictions in the development of ESG matters, with implications for multinational entities operating in Italy that will have to align with ESG requirements imposed by the domestic regulatory system.

In the medium term:

- First cases of “greenwashing” and ESG litigation, mediation and enforcement by authorities.
- Emergence of more competitive entities that will have adopted more rigorous and robust approaches to ESG matters, such as through the implementation of *ad hoc* safeguards and appropriate measurement and reporting systems.

In the long term:

- Entry into force of the proposed CSDD Directive and further development of the EU and Italian regulatory framework on ESG, with eventually the definition of a globally aligned ESG framework of standards mandatory for an increasing number of recipients and intended to govern several corporate aspects (i.e., ESG Due diligence, risk management, sustainable governance, ratings, labelling, disclosure, etc.).
- Emergence of more competitive entities that will have anticipated the entry into force of norms and the development of best practices in the ESG area.

AUTHOR BIOGRAPHIES



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Roberto Randazzo is responsible for the ESG and Impact industry. With a background in commercial and corporate law, he has developed transversal expertise in sustainability, ESG criteria, impact finance and social innovation, assisting investment funds, benefit corporations, B-Corps, and companies interested in generating positive and measurable impacts. For more than 20 years, Roberto has also been involved in non-profit organisations, strategic philanthropy and social entrepreneurship, dealing with projects both nationally and internationally, with focus on emerging markets, and in particular those in Sub-Saharan Africa. He has always combined professional and academic activities, and is currently an Adjunct Professor at Tiresia - Politecnico di Milano and a member of the Extended faculty of MIP - Politecnico di Milano. Roberto is also the outgoing Chairman of esela - The legal network for social impact, Officer of the Business Human Rights Committee of the International Bar Association and Advisor of OECD; he is member of the scientific committees of Ashoka Italia, Salone della CSR and Social Impact Agenda for Italy and of the editorial board of the magazine “Cooperative ed Enti Non Profit”. Since 2012, Roberto has been Honorary Consul of the Republic of Uganda in Milan and Northern Italy.

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JAPAN

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Law Over Borders Comparative Guide 2023

www.globallegalpost.com/lawoverborders

1. How is “ESG” in Japan defined in a corporate/commercial context, and what are its major elements?

ESG is not defined under laws such as the Companies Act. Corporate Governance Codes (codes incorporated into the rules of stock exchanges that apply to listed companies) only stipulate specific matters related to ESG and do not define ESG itself. Furthermore, there is no specific definition in the commercial context.

There is no clear indication of which aspects of ESG are particularly emphasized in Japan. Traditionally, corporate governance has been actively discussed from the perspective of preventing corporate scandals. At the time of the establishment of the Corporate Governance Code in 2015, “G” was also a central issue.

Since then, with the global trend toward stronger environmental initiatives and emphasis on human capital, there has been a growing interest in “E” (such as climate change) and “S” (such as diversity in Japan).

2. What, if any, are the major laws/regulations in Japan specifically related to ESG?

There are no laws or ordinances in Japan that can be referred to as ESG-related laws or ordinances that correspond to, for example, the EU’s Sustainable Finance Disclosure Regulation, the UK FSA’s regulations implementing Task Force on Climate-Related Financial Disclosures (TCFD), France’s Vigilance Law or Germany’s Supply Chain Due Diligence Act. Currently, discussions on the inclusion of sustainability disclosures in securities reports are being conducted by the working group of the Council of Financial Services Agency (FSA).

There are, however, regulations covering the individual elements of “E”, “S” and “G”, as discussed further below in Question 3.

3. What other laws/regulations in Japan touch on ESG themes?

Companies Act

The Companies Act stipulates the basic matters relating to corporate governance. There have been a series of amendments regarding institutional design, directors’ responsibilities and disclosures to improve corporate governance. An amendment to the Companies Act in 2021 expanded the inclusion of director remuneration and outside directors in business reports.

Financial Instruments and Exchange Act

The Financial Instruments and Exchange Act stipulates the disclosure of securities reports and other information in accordance with the Cabinet Office Ordinance based on such Act, primarily in relation to listed companies. In addition to the disclosure of financial information, disclosure of governance is also stipulated. Recently, the amendment of the Cabinet Office Ordinance on the Disclosure of Corporate Affairs based on the Financial Instruments and Exchange Act in 2019 expanded the disclosure content of annual securities reports to include an overview of corporate governance, the status of directors and auditors, executive compensation amongst others.

Offense of Bribery of Foreign Public Officials (under the Unfair Competition Prevention Act)

This crime was established to prevent illegal benefits from being given to foreign public officials in international trade. Revised in May 2004, the crime, which had been limited to punishment of acts committed in Japan, was amended to make the offering or giving of bribes overseas by Japanese nationals also punishable. In addition, Guidelines for the Prevention of Bribery of Foreign Public Officials have been provided to assist companies in taking a voluntary and preventive approach.

Antimonopoly Act

When collaborations and agreements are made between companies for environmental measures, the issue is to what extent such collaborations and agreements should be regarded as illegal cartels from the viewpoint of the Antimonopoly Act. There may be a view that collaborations and agreements that are effective for environmental measures should not be illegal under the Antimonopoly Act. Japan's Antimonopoly Act does not provide for sustainability to be taken into account in the context of cartels, as a general rule. However, guidelines for specific areas (e.g., recycling guidelines and guidelines for joint R&D) from this perspective are stipulated.

Labor-related laws (such as Labor Standards Act, Labor Contract Act, etc.)

Workers' rights are protected by a series of labor-related laws. For example, the Labor Standards Act protects workers' rights and stipulates labor standards that employers must comply with.

Act on Securing, Etc. of Equal Opportunity and Treatment between Men and Women in Employment (so-called Equal Employment Opportunity Act)

This law provides for the prohibition of gender-based discrimination in the field of employment.

Act on Promotion of Measures to Cope with Global Warming

The Act on Promotion of Measures to Cope with Global Warming, established in 1998, was amended in 2021 to specify the goal of achieving a decarbonized society by 2050. The law stipulates the measures to be taken by national and local governments to address climate change, as well as the obligations of citizens and businesses to make efforts to take measures controlling greenhouse gas emissions (e.g., the effort (1) to choose the equipment which contributes to the reduction of greenhouse gas emissions and to use the equipment in a manner that reduces greenhouse gas emissions as much as possible (for citizens, in their daily life; for businesses, in their business activities) and (2) to manufacture, import, sell or provide products or services that emit less greenhouse gases and to provide accurate and appropriate information on the greenhouse gas emissions associated with the use of such products (for businesses in their business activities)) and to cooperate with the measures taken by national and local governments. Companies that emit more than a certain amount of greenhouse gases are obliged to report emissions information, which is then compiled and published by the Minister of the Environment.

Climate Change Adaptation Act

The Climate Change Adaptation Act, effective 30 November, 2018, stipulates the formulation of climate change plans by the government and local governments, as well as the implementation of measures to collect and provide information on adaptation to climate change.

4. What, if any, litigation or enforcement activity has Japan seen related to ESG?

At present, there are no specific legal procedures to prevent greenwashing. However, punishment for acts such as the making of false statements in a securities report, for example, may be imposed by general regulations. The FSA of Japan is currently considering revising its guidelines for supervision of financial instruments business operators to prevent greenwashing, but such guidelines have no legal enforceability (see Question 5 in relation to soft non-binding laws).

5. What are the major non-law/regulatory drivers of ESG trends and developments in Japan?

Soft non-binding laws

Corporate Governance Code

The listing rules of the stock exchange stipulate that companies must comply with the Corporate Governance Code or explain why if they do not (“comply or explain”), and each listed company discloses this information in its corporate governance report. The Corporate Governance Code requires listed companies to appropriately disclose their sustainability initiatives, including consideration of environmental issues, respect for human rights and the working environment for employees. In particular, companies listed on the Prime Market have been required to disclose their initiatives based on TCFD since April 2022.

Action Plan on “Business and Human Rights” (2020-2025)

This was formulated on October 16, 2020 at the related ministries and agencies liaison conference in the government.

It was formulated to ensure the steady performance of the “Guiding Principles on Business and Human Rights” endorsed in the resolutions relevant to the UN Human Rights Council in 2011. It is also regarded as one of the initiatives to realize the Sustainable Development Goals (SDGs).

Guidelines for Human Capital Visualization

Guidelines for human capital visibility (i.e. disclosure) were published on August 30, 2022, setting forth the methods and steps for visualization.

Basic guidelines for calculating greenhouse gas emissions throughout the supply chain

In March 2012, the Ministry of the Environment presented a concept for business entities to calculate emissions emanating from the supply chain.

Efforts to address the issue of greenwashing of ESG investment trusts

In May 2022, the FSA published the “Advanced Asset Management Progress Report 2022.” In the report, the FSA stated that, once an investment trust emphasizes “considering ESG elements” as features of the product or its investment policy, the asset management company for such investment trust should continuously strengthen their investment processes and approaches and provide clear explanations and disclosures in a consistent manner in line with the actual condition of the investment process so that customers can make investment decisions appropriately.

In addition, the “New Capitalism Follow-up” released by the Cabinet Secretariat in June 2022 stated that the FSA’s guidelines for supervision of asset management companies will be revised by the end of 2022 in order to improve the reliability of the ESG market.

Stakeholders

General public

While individual investors are involved in ESG on their own, general awareness of investing in ESG is growing. A survey conducted by Nomura Asset Management, one of major investment managers in Japan in 2020, showed that 52% of those who own stocks and mutual funds said they are interested in ESG investments.

Institutional Investors

In 2015, the GPIF, one of the world’s largest pension funds, signed the Principles for Responsible Investment (PRI), and many institutions in Japan followed their example (119 institutions have signed as of 10 October, 2022). Many institutional investors have accepted the Japanese Stewardship Code established in 2014, and many institutional investors have been making ESG investments in recent years because of the Code’s March 2020 revision, which requires considerations of sustainability. The code refers to the Stewardship responsibility as “the responsibility of qualified institutional investors to increase the medium and long-term investment returns of their clients and beneficiaries (including ultimate beneficiaries) by promoting the enhancement of corporate value and sustainable growth of the Japanese companies in which they invest through constructive “dialogue with a purpose” (engagement) based on a deep understanding of the companies and their business environment, as well as considerations of *sustainability* in accordance with the investment strategy.”

Companies

Listed companies in particular have been increasing their interest and investment in ESG in recent years. In response to the Corporate Governance Code, the company is working to address issues surrounding sustainability, including compliance with the TCFD, respect for human rights, consideration for the working environment and fair and appropriate treatment of employees.

As listed companies, which are relatively large companies, are responding to ESG, including in respect of their supply chains, small and medium-sized enterprises (SMEs) in those supply chains are also being asked to address ESG issues.

Government

The Government has announced the promotion of ESG investment in various official documents. Various ministries and agencies are working on ESG in a cross-sectional manner. The scope of corporate information to be disclosed with regard to the status of corporate governance has been expanded by the revision of the Companies Act by the Ministry of Justice, as well as the revision of the Financial Instruments and Exchange Act by the FSA. The Ministry of the Environment is making efforts to improve the environment. As a member of NGFS (Network for Greening the Financial System), the FSA of Japan has been encouraging financial institutions to analyze climate-change scenarios. The Ministry of Health, Labor and Welfare is working on the rights of workers, women and persons with disabilities. The Ministry of Economy, Trade and Industry (METI) is promoting disclosure based on the TCFD framework.

National Contact Points (NCPs)

Organizations such as the OECD's National Contact Points do not exist in Japan for ESG. The following ministries and agencies carry out their respective activities, as follows:

- the FSA (for ESG investment);
- the Ministry of the Environment (for the environment);
- the Ministry of Health, Labour and Welfare (for social, dealing with welfare of workers, women, persons with disabilities and children etc.); and
- the Ministry of Justice (for human rights, dealing with human rights consultation, relief procedures, human rights enlightenment activities etc.).

TCFD Consortium

TCFD Consortium, a private-sector organization, was established in 2015 and is regarded as a forum for companies and financial institutions who endorse TCFD's recommendations to work together to promote initiatives and discuss them.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

The laws and regulations listed in Question 2 relate to disclosure of "G." Some disclosures listed in Question 3 above focus on outcome and others focus on processes. For example, the Act on Promotion of Measures to Cope with Global Warming focuses on outcome in obliging certain companies to disclose their emissions.

Reporting

ESG disclosures are made in the integrated reports issued by many listed companies, as well as in securities reports and business reports. They are usually reported annually.

Although there are no legally prescribed indicators to be used for ESG disclosure, the corporate governance codes require appropriate responses to sustainability issues. In particular, the TSE Prime Market requires disclosure based on the recommendations of TCFD from April 2022. According to a survey conducted by GPIF between January and March 2022 (more than 700 companies, or about one-third of the companies listed on the First Section of the Tokyo Stock Exchange,

responded), the number of companies making TCFD disclosures increased to 249 from 139 in the previous year's survey.

Consideration for double materiality in disclosures is not necessarily emphasized at the present time. Although the TCFD-based response requires disclosure of the financial impact of climate change, consideration of the company's impact on the environment and society as a whole, while considered in the scenario analysis, does not yet appear to be sufficient.

7. Which sectors are most impacted by ESG in Japan? How significant is ESG investment in Japan?

Private equity

ESG investment is considered important in the private equity sector. For Universal Owners, the improvement of global environmental and social issues is of more concern than the performance of a particular company. In their private equity investments through investments in private equity funds, which are growing as alternative asset investments among Japanese major asset owners, many Universal Owners, like GPIF, appoint investment managers by taking into consideration their engagement with ESG and the integration of ESG considerations in their investment analyzes and decision-making processes.

Smaller investors try to differentiate themselves by focusing on specific asset classes. They may invest in companies with low ESG awareness and subsequently work to improve their ESG aspects to enhance their company's value.

Hedge funds/asset managers

Hedge funds, which usually pursue short-term gains, seem to be incompatible with ESG investments, which pursue medium to long-term gains. However, UNPRI published a guide to ESG incorporation in hedge funds in May 2020, which showed that asset owners emphasizing ESG may have fund managers incorporate ESG factors into hedge fund strategies, and it is thought that there will be similar management among Japanese asset owners as well.

Banks

Efforts continue to promote ESG finance, i.e., investment and financing activities that emphasize a long-term perspective for corporate analysis and evaluation and take ESG information into account. One of the core components of ESG finance is financing for renewable energy issuance projects. Given Japan's heavy reliance on coal-fired power generation as well as oil and Liquefied Natural Gas (LNG), the climate change risk of energy-related financing is not small for banks. Sustainability finance is becoming more and more important in promoting transitions in these industries.

Small and medium-sized enterprises (SMEs)

As discussed in Question 5 (Stakeholders: Companies), as listed companies are responding to ESG, including in respect to their supply chains, SMEs in those supply chains are also being asked to address ESG issues. ESG-conscious management is gradually growing among SMEs.

Fashion

There are ESG-related issues, such as the heavy environmental burden in the production and transportation processes, the mass disposal of clothing due to the shortening of the lifecycle of clothing and human rights problems in manufacturing in foreign countries. As corporate brand image is very important in the fashion sector, interest in ESG is very high.

Travel industry

Restrictions on the movement of people caused by COVID-19 have hurt the travel industry, but as it continues to recover, it is increasingly important to ensure clients' health and safety. As nature is an important tourism resource, it is also necessary to prevent environmental destruction caused by travel.

Automobile industry

The automobile industry has a history of responding to environmental regulations, and in recent years, there has been a shift to electric vehicles. Some countries have declared a ban on the sale of internal combustion engine cars, but Japan has not reached that point. However, it is thought that the trend toward zero emissions will not change, and companies will be required to act.

In addition, automobile manufacturers are characterized by a supply chain that includes numerous component suppliers, and therefore, they need to take initiatives that include the supply chain.

Energy industry

TCFD designates an energy industry sector as one of the four sectors in non-financial sector that is strongly affected by climate change (p13 of "Recommendations of the Task Force on Climate-related Financial Disclosures (June 2017)"), and the disclosure items for the energy industry companies are clarified in the Supplemental Guidance. Companies in the energy industry sector in Japan take into account these items when they prepare TCFD disclosures.

In Japan, the question of whether to restart nuclear power plants, which have largely ceased operation since the Great East Japan Earthquake in 2011, and the development of renewable energy are areas of interest, which are greatly influenced by ESG policies.

METI will formulate a process chart for electric power and gas as the industries with high carbon dioxide emissions by the end of 2022, which will describe the outlook for technological development and emission reduction rates for each industry and support financing for transitions.

Real estate industry

ESG investment is said to be lagging in the domestic real estate sector (in terms of sustainable investment measured by asset, real estate investment accounted for about 2.3% in 2020), and it is expected that further efforts will be made on themes such as the improvement of health and comfort, disaster prevention measures, contribution to local communities, improvement of energy conservation performance (improvement of performance of air conditioners,

water conservation, etc.) and utilization of renewable energy. The number of real estate funds participating in GRESB, which is an independent organization providing validated ESG performance data and peer benchmarks for investors and managers, is increasing. GPIF joined GRESB in March 2020.

E-commerce

Interest in ESG is also high in the e-commerce sector. According to a survey in 2022, 30% of e-commerce companies consider ESG/the SDGs as an important issue. Efforts are being made to reduce carbon dioxide, such as using a delivery method that leaves packages at the recipient's door in order to prevent the additional emissions caused by re-delivery.

Game industry

In the Japanese game industry, ESG does not seem to be a major topic, but efforts to improve the work-life balance of game creators are spreading.

8. What are the trends in Japan regarding ESG governance?

Although a Chief Sustainable Finance Officer at the FSA of Japan was appointed on 15 March, 2019, the appointment of a chief sustainable officer is not common in private companies. However, persons in charge of ESG and alignment with the SDGs are often appointed from among directors and executive officers.

There is a growing trend for companies to establish organizations to promote ESG, with 55 companies among the Nikkei JPX-400 having established internal committees for ESG in 2020. However, unlike in Europe and the U.S., where committees directly under the board of directors with the participation of outside directors are the norm, executive officers that report to the board of directors are common in Japan.

At present, discussions regarding ESG-related fiduciary obligations are not evolving in corporate law, trust law or pension law. It has been pointed out that in corporate pension funds, for example, ESG investment cannot always be actively implemented from the viewpoint of fiduciary responsibility, since it is not clear whether ESG investment will necessarily contribute to maximizing the interests of beneficiaries.

9. To what extent are ESG ratings or ESG benchmarks relied upon in Japan?

ESG rating agencies

S&P, Moody's and Fitch are all registered as credit rating agencies under the Financial Instruments and Exchange Act and are widely used by companies and investors. There are eight registered credit rating agencies, including S&P, Moody's and Fitch (two Moody's, two S&Ps and Fitch).

ESG benchmarks

The MSCI World SRI Index, Sustainalytics and ESG Benchmarks are all shown on the website of the Japan Exchange Group and are used by Japanese companies and investors.

10. What is the role of the private markets versus public markets in driving ESG developments in Japan?

Private companies

Privately held companies are sometimes asked to act for ESG by business partners who are listed companies, to represent and warrant that they and their subcontractors comply with international laws with regard to ESG matters such as human rights, embargoes, terrorism, the health and safety of employees and third parties, environmental protection, corruption and bribery, and even request to let them know the result of the assessment by Sedex and Ecovadis, which assess ESG matters such as business ethics, labor practices, securities and environment. In addition, ESG issues are being incorporated in the initiatives private companies are making with respect to the SDGs, particularly when voluntarily re-examining their business models. Such initiatives are often difficult to quantify.

Public companies

Many listed companies are generally proactive in addressing ESG issues, however, developments remain in their early stages. Many listed companies currently prepare integrated reports that exhibit financial and non-financial information relating to ESG and describe the active approach to ESG within the business. Although many listed companies compile integrated reports (a private survey reported 641 companies prepared their integrated reports in 2021), some point out that the content does not show the quantitative impact of ESG information on financial information, or that disclosure materials other than integrated reports (such as medium-term business plans) do not include ESG information.

Government-owned organizations

While ESG considerations are important for government-owned organizations, they do not materially differ from those for other companies.

ESG agenda

The ESG agenda is promoted in Japan. In 2016, SDGs Promotion Headquarters, headed by the Prime Minister, was established, and a system was set up to take the lead in both domestic implementation and international cooperation. Ministries, Agencies and other relevant organizations are also making efforts to achieve SDGs. In Japan, it is generally recognized that ESG investment is one of the approaches to solving social issues and facilitates the achievement of SDGs. GPIF states that, since the solution of social issues creates business/investment opportunities, companies taking on SDGs would be able to ensure sustainable growth in their corporate value. Thus, ESG investment is targeted at a wide range of social issues, including SDGs (e.g. gender equality, affordable and clean energy, and climate action). In line with the international trends with regard to the conduct of the ESG evaluation/data provider, such as IOSCO's 2021 report entitled "Environmental, Social and Governance (ESG) Ratings and Data Product Providers Final Report," the FSA of Japan published, on 12 July, 2020, a draft "Code of Conduct for ESG Evaluation and Data Providers," which summarizes the current status of ESG evaluation and data provision, and issues in view of future market development while also proposing specific actions

expected to be taken by ESG evaluation/data providers. The Code is expected to be disseminated as soft non-binding law.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

There are no comprehensive ESG regulations in Japan, and standards for information disclosure regarding ESG have not been established. Individual companies' initiatives will not fill the gap. It is difficult even for institutional investors to establish appropriate valuation methods for ESG investments. In addition, it is not clear whether ESG investment will necessarily contribute to maximizing the interests of beneficiaries. Therefore, in corporate pensions, for example, ESG investment cannot be actively implemented from the viewpoint of trustee liability (only five domestic corporate pension plans are signatories to the PRI). Furthermore, it is difficult to introduce "green investment" straight away in Japanese industry, a large proportion of which is said to be difficult to decarbonize. It may be more realistic to expect a gradual transition towards decarbonization, as companies begin to engage with low-carbon initiatives.

Although there are no standards for greenwashing, the FSA plans to establish guidelines for the supervision of asset management companies by the end of 2022.

12. What information sources are most relevant for ESG considerations in Japan?

In Japan, international frameworks such as the TCFD, Global Reporting Initiative (GRI) and CDP have been introduced and applied to Japanese companies. While there are no major decision-making frameworks that are unique to Japan, some domestic guidance has been developed, such as the "Guidance on Climate Change Information Activities to Promote Green Investment" (providing a perspective on importing disclosure information based on TCFD recommendations). The Sustainability Standards Committee was established within the Financial Accounting Standards Foundation, a public interest incorporated foundation that develops Japanese accounting standards, but no domestic standards have yet been created.

The Japan stock exchange (JPX) has established a website called JPX ESG Knowledge Hub, on which it disseminates ESG information, such as ESG guidebooks, seminars and other activities for listed companies and institutional investors (the website is for the domestic market and in Japanese only, JPX has other webpages regarding ESG in English).

Established in 2015, TCFD Consortium is a forum for companies and financial institutions that endorse TCFD recommendations to work together to promote initiatives and discuss them.

13. Has Japan developed a Taxonomy related to ESG?

Not currently.

14. What does the future hold for ESG in Japan?

In Japan, in response to the growing international interest and debate on ESG, the government has been developing systems to enhance, and companies are working on, the furthering of ESG disclosure. Since domestic interest is very high, the response to ESG is expected to progress considerably in the short term. The government is also considering measures to deal with greenwashing.

In Japanese domestic industry, where the decarbonization of a large proportion of the industrial and energy sectors is considered difficult, such transition is likely to be focused for the time being, but will likely gradually move toward broader green investment. As long-term perspectives are indispensable for tackling decarbonization, it is expected that initiatives from an environmental perspective will be carried out over the long term. Furthermore, in the long run, the impact of corporate activities on the environment and society (double materiality) will also likely be increasingly taken into account.

AUTHOR BIOGRAPHIES



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MEXICO

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Law Over Borders Comparative Guide 2023

www.globallegalpost.com/lawoverborders

1. How is “ESG” in Mexico defined in a corporate/commercial context, and what are its major elements?

There is no definition of ESG in the Mexican legal system, and direct references to ESG in laws and regulations are very limited. Regulation on ESG matters is scarce when compared to other jurisdictions (especially the U.S. and the European Union).

Mexican companies are increasingly using ESG as a management tool to identify and mitigate material risks regarding environmental, social and governance matters, as well as to identify opportunities in those areas. Through an increased ESG focus, Mexican companies are gaining better access to commercial and financial opportunities, such as becoming preferred suppliers of clients with ESG commitments or accessing broader pools of ESG-conscious investors and lenders.

ESG matters can be found across multiple sources of the Mexican legal system. Recently, certain ESG-related matters have attracted special attention from regulators, companies, investors and other market participants, as they are “hot topics”. Among those matters are the environmental and social impact of projects (water availability, pollution, rights of indigenous communities, etc.), labor rights and working conditions, anti-corruption and money laundering prevention, as well as personal data protection and cybersecurity.

2. What, if any, are the major laws/regulations in Mexico specifically related to ESG?

ESG principles and obligations are not compiled or codified. ESG-related provisions can be found across numerous laws and regulations for the three levels of government (i.e., federal, local and municipal), the most relevant being the Federal Constitution, which serves as the basis for human rights, including the right to a clean environment and labor rights.

3. What other laws/regulations in Mexico touch on ESG themes?

Environmental matters, such as climate change, energy transition, use of natural resources and environmental impact of projects are included in, among others:

- the National Waters Law;
- the General Law of Ecological Equilibrium and Environmental Protection and its secondary regulations;
- the General Climate Change Law;
- the General Law on the Circular Economy;
- the Energy Transition Law; and
- the General Law for the Sustainable Forest Development.

Social matters, such as labor relations and working conditions, business and human rights and indigenous people’s rights are included in, among others:

- the Federal Labor Law and its secondary regulations;
- the National Security Law; and
- the National Institute of Indigenous People’s Law.

Governance matters are included in, among others:

- the General Law of Commercial Companies;
- the Securities Market Law;

- the General Law of the National Anti-corruption System;
- the Federal Criminal Code; and
- the Federal Tax Code.

Mexico is also a signatory to many international treaties on ESG-related subjects, such as human and labor rights. This is particularly relevant as, under Mexico's constitutional law, international treaties are equivalent to federal law from a hierarchy standpoint.

Additionally, there are several "comply or explain" guidelines (soft law) that touch upon ESG-related matters. These include the Corporate Governance Code of Principles and Best Practices issued by the Business Coordinating Council, and the Sustainability Guide issued by the Mexican Stock Exchange. The Mexican Council for Sustainable Finance (formerly known as the Green Finance Advisory Council) has also issued the Green Bonds Principles.

In October 2020, Senator Germán Martínez (formerly, of Morena party) presented a comprehensive bill of law on corporate responsibility and due diligence obligations. The bill has had no legislative movement in Federal Congress.

4. What, if any, litigation or enforcement activity has Mexico seen related to ESG?

Litigation and enforcement of ESG-related matters have become more prevalent in the past five years. However, the level is minimal when compared to other jurisdictions where ESG frameworks are more developed, especially the European Union and the United States.

Recently, infrastructure and energy projects have been suspended or canceled based on environmental and social claims. Regarding energy projects, some have failed due to the lack of compliance with environmental and social impact assessments required by law, or due to irregular indigenous consultations that contravene the Indigenous and Tribal Peoples Convention. For example, recently, Constellation Brands (owner of the Corona beer brand in the U.S.) located in the city of Mexicali (Baja California, Mexico), was forced to cancel the construction of a brewery due to concerns regarding the scarce availability of water and potential harm to local communities and the environment. Furthermore, federal courts often issue injunctions to prevent energy and infrastructure construction projects, on the grounds of developers' alleged breaches of environmental laws, damage to cultural heritage or failure to comply with commitments made towards local communities during the approval process.

In early August 2022, 10 workers were trapped in a collapsed mine in the State of Coahuila. Among other relevant facts, the media, and the Mexican government, called attention to the miners' lack of social security and the general conditions in which they were forced to perform their duties. Further, during the criminal investigations the miners' incapacity to unionize was consistently cited. Foreign mining companies are currently under heavy scrutiny, and permits have been revoked on grounds of non-compliance with labor and administrative regulations. These sanctions are, in some cases, parallel to ongoing criminal investigations.

The labor chapter of the United States–Mexico–Canada Agreement (USMCA) is also a source of enforcement actions. For example, several manufacturing companies (including Panasonic and Tridonex) were recently investigated due to allegations made by workers in the border state of Tamaulipas (Mexico), arguing they were being denied their right to unionize. We expect that the labor chapter of the USMCA will continue to gain relevance and traction, to a great extent driven by US labor unions, which will result in further enforcement actions.

Private enforcement is also present and growing. It is increasingly common for financial institutions and companies to include ESG-related provisions in agreements entered into with customers and suppliers to ensure acknowledgement and compliance with certain standards. Breach of such provisions often results in termination and indemnification rights. These provisions are mostly related to anti-corruption, environmental performance and waste management, as well as labor conditions in the supply chain.

We have also seen private enforcement through post M&A litigation related to indemnification rights arising from the breach of ESG-related provisions by target companies.

5. What are the major non-law/regulatory drivers of ESG trends and developments in Mexico?

ESG in Mexico is primarily driven by market forces, not regulation.

The adoption of ESG strategies by Mexican and multinational companies with a presence in Mexico has been an important driver of trends and developments. In many cases, adoption is voluntary, and ESG is used as a management tool to mitigate risk and to improve the performance of a company. In other cases, the adoption of an ESG strategy derives from commitments with financial institutions or major clients, a reaction to competitors' successful positioning as ESG-conscious firms or because they are subsidiaries of companies subject to ESG obligations in a different jurisdiction.

Financial institutions and institutional investors (especially those with global footprint) are important promoters of ESG. The Mexican Stock Exchange (BMV) and the Institutional Stock Exchange (BIVA), are also key promoters. For example, the BMV has created an ESG Index; and BIVA, has actively promoted the adoption of ESG principles among companies with listed securities, as well as the ESG-themed bond issuances. Moreover, BIVA recently launched "BIVASG", an information distribution tool that provides relevant and up-to-date information on methodologies, regulatory changes and securities transactions that comply with ESG principles. It also compiles ESG-related information of registered issuers in Mexico.

The Mexican Council for Sustainable Finance, consisting of representatives from the Mexican financial sector, seeks to promote the financing of projects that have a positive impact on sustainability, and is also a relevant stakeholder. They have been an active promoter of best practices in green and other types of sustainable finance in past years.

Non-binding principles and guidelines (soft laws) are also drivers of ESG trends in Mexico, including both domestic and international sources. Among

the most relevant domestic sources are the Corporate Governance Code of Principles and Best Practices issued by the Business Coordinating Council, and the Sustainability Guide issued by the BMV. International instruments such as the Equator Principles and the Global Reporting Initiative (GRI) have influenced the design, implementation and reporting of ESG strategies and programs in Mexico.

Likewise, the Mexican financial regulators have recently published soft law guidelines to achieve a higher level of compliance with certain matters. For example, the Minimal Suggested Criteria to Hire Cloud Computing Services that Deal with Personal Data has been issued by the National Institute of Access to Information. The General Anti-Corruption Prosecutor's Office is expected to publish the Anti-Corruption Guidelines in the near future.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

Provisions related to corporate disclosure on ESG matters are extremely limited in Mexico.

However, companies that are listed as issuers on a stock exchange must issue annual reports covering certain basic ESG information, such as the following:

- activities in which they engage that could represent an environmental risk, and the measures that are being taken to mitigate it;
- corporate structure and processes, (e.g., standard information on shareholders and relevant officers); and
- the number of employees and percentage of unionized workers.

Additionally, private companies must report on certain ESG-related matters as a part of ordinary procedures and regulatory verifications, especially in labor and environmental matters. However, such disclosure is often non-public and addressed exclusively to the authorities, such as the Ministry of Environment and Natural Resources and the Ministry of Labor and Social Welfare.

7. Which sectors are most impacted by ESG in Mexico? How significant is ESG investment in Mexico?

ESG investment, as well as green and sustainable finance, has been growing. For example, according to the Mexican Council for Sustainable Finance, the funds raised through the issuance of green and other types of sustainable bonds in 2022 (245 billion pesos or 12.2 billion dollars, approximately) was 30% higher than in 2021 (185 billion pesos or 9.2 billion dollars, approximately) and 24 times higher when compared to pre-pandemic levels (2019). Sovereign sustainable bonds issued by the Mexican government played an important role in 2022 (approximately 40% of the total funds raised).

ESG has impacted many sectors and industries in Mexico. Due to Mexico's current social and political context, certain topics and industries have attracted more attention than others. In our experience, the sectors that have been most impacted by ESG in Mexico are as follows.

Retirement and pension funds

Certain asset managers, such as the Mexican retirement fund managers (AFOREs) and investment companies specialized in retirement funds (SIEFOREs), are required to disclose information on how they incorporate ESG criteria into their investment strategies, pursuant to regulations that came into effect in 2022 (i.e., the General Provisions in Financial Matters for the Retirement Fund Managers, as amended).

Early in 2022, the Mexican Association of Retirement Funds Managers (AMAFORE) announced it is working on an ESG taxonomy that would apply to Mexican AFOREs and SEIEFOREs. This taxonomy is set to define certain ESG investment metrics, and to ensure that the investments selected by such AFOREs and SIEFOREs meet certain ESG criteria.

Banking and finance

The banking and finance industry has been one of the most active regarding ESG by promoting green and sustainable finance. It is increasingly common for banks to include provisions regarding certain ESG-related matters (e.g., anti-corruption and labor practices) in financing agreements. Foreign-owned banks operating in Mexico brought this practice to Mexico, but it has now been adopted by Mexican banks and other financial institutions, who are also incorporating ESG in their day-to-day operations.

Additionally, the Mexican Council for Sustainable Finance promotes green and sustainable finance in Mexico. This body has engaged in important efforts to issue guidelines (such as the Green Bonds Principles) that companies can use to achieve financing based on ESG criteria.

Infrastructure and energy

ESG has become increasingly relevant in infrastructure and energy projects, especially regarding environmental and social matters. Its impact is assessed by the three levels of government and by companies in all the phases of such projects (i.e., during the approval, construction and operation). It is especially relevant for companies engaging in this sector to design a robust ESG strategy, which should incorporate topics such as inclusion of local communities, protection of indigenous rights, lands and cultural heritage sites, environmental protection and anti-corruption.

Real estate

The real estate industry has also been impacted by ESG in the past few years, especially regarding environmental protection and social responsibility of project development. Real estate companies now tend to complete environmental and social impact studies prior to the commencement of projects, even if it is not mandatory. This often means obtaining certain certifications by third parties in relation with sustainability goals set up for a determined project. In practice, no major real estate project can be successfully accomplished without ensuring that local communities will benefit, whether through employment, renovation of natural resources or infrastructure.

Consumer goods

Consumer goods companies are paying special attention to environmental matters linked to their production process, such as the level of their emissions and carbon footprint, as well as waste and water management. These subjects are also garnering increased attention from regulators and other stakeholders. Additionally, the mitigation of risks related to product liability has received greater attention recently.

E-commerce

E-commerce is rapidly growing in Mexico and has also been impacted by ESG, especially in relation to governance for data protection and cybersecurity matters. Companies in this sector are highly exposed to risks related to the personal data they control, and are therefore engaging in efforts to design an efficient data protection strategy to mitigate risks.

8. What are the trends in Mexico regarding ESG governance?

Board attention to ESG-related matters has grown over the past few years. Under Mexican law, the board of directors is responsible for supervising a company's risk management and ESG is ultimately about managing risk. It is common practice for the board to be supported by committees (e.g., an audit committee and a sustainability committee), entrusted with specific responsibilities regarding the ESG strategy.

Mexican companies frequently appoint their Chief Sustainability Officer (CSO) as ESG lead, in charge of coordinating internal efforts by multiple corporate functions. At the same time, the involvement of legal counsel (both internal and external) is becoming more relevant in the design, implementation and reporting of ESG initiatives. Governance is typically overseen by legal counsel, and good governance is required for an effective ESG program.

Supply chain liability is not sufficiently developed in Mexico. However, we have noticed recently that multinational business-to-business companies are increasingly requiring their suppliers to agree contractually to adopt ESG-related measures in their operations (e.g., product safety, environmental performance, labor and working conditions). This is also the case for subsidiaries of foreign companies, especially from certain countries of the European Union. Given Mexico's importance in the global supply chain of many sectors (automotive, aeronautical, electronics and health care devices, for example), Mexican manufacturers are implementing ESG initiatives and reporting systems at an accelerated pace to meet client demands.

Finally, there is an increasing private litigation activity regarding breaches of ESG-related contractual obligations. Some of these cases are related to breaches of labor provisions (e.g., health and safety) contained in both the USMCA and Mexican law. We expect that these matters will become even more relevant in the upcoming years.

9. To what extent are ESG ratings or ESG benchmarks relied upon in Mexico?

ESG rating agencies

ESG rating agencies have presence in Mexico, and companies are increasingly

referring to ESG ratings in their disclosure documents. Sistema B and SDG Action Manager show an increasing presence in Mexico. Both companies certify that companies implement business models that center on environmental, transparency, social and labor impact. Currently, more than 60 Mexican companies are certified B Companies. These companies include those specializing in services, finance and agriculture, among others.

The engagement of ESG ratings companies is also relevant, as they are used as part of the process to issue green and other types of sustainable bonds.

ESG benchmarks

The ESG Index, launched in 2020 by the BMV jointly with Standard & Poor's is the best example of an ESG benchmark in Mexico. This index provides information regarding certain Mexican listed companies that comply with certain ESG metrics, and its objective is to promote ESG investing among the general public. Currently, this ESG Index is comprised of 29 companies from different sectors.

10. What is the role of the private markets versus public markets in driving ESG developments in Mexico?

Private companies

Mexican private companies that are actively designing and implementing ESG strategies in their processes are mostly doing so to mitigate potential risks. Likewise, they are engaging in these efforts to comply with requirements made by their clients, lenders and investors. To achieve this, they are committing to adopt positive environmental goals beyond what is required by the applicable legal provisions, and engaging in actions that have a positive social impact, such as adopting specific commitments in diversity and inclusion.

Public companies

ESG is becoming relevant item in the agenda of Mexican public companies' boards, and boards are increasingly being asked to explain the company's ESG position (or lack thereof).

Public companies are tackling ESG issues, as a good ESG record provides greater financing opportunities. Mexican public companies have controlling shareholders (or controlling groups) and governance issues have been a matter of special interest since the enactment of the amended Securities Market Law in late 2005. For example, since 2006 Mexican public companies must have board committees entrusted with corporate governance and audit functions, as well as appoint a percentage of independent directors on their board. Moreover, there are several "comply or explain" guidelines (soft law) included in the Corporate Governance Code of Principles and Best Practices issued by the Business Coordinating Council. However, stakeholders' demands for increased diversity and inclusion at the board or top management level is a relatively new subject and have not been elevated to legal status.

Moreover, public companies are achieving a certain level of compliance based on the Sustainability Guide issued by the BMV. This guide provides voluntary guidelines and recommendations for Mexican public companies, based on diverse domestic and international sustainability frameworks.

Adopting ESG measures is promoted by market participants. For example, BIVA recently launched the Chief Sustainability Officer (CSO) Acceleration Program. This program seeks to promote the adoption of ESG criteria in listed companies by advising their ESG leaders in the design and adoption of their strategy. Likewise, the program seeks to provide general advice for companies to obtain investment through an ESG-related strategy.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

The first challenge is where to start and how to prioritize ESG issues. The starting point is to have a robust materiality analysis prepared with the support of an expert (internal or external). The outcome will provide information for the company to decide where to focus its efforts.

Defining the role of the board can also be challenging. Since the board is ultimately responsible for the company's risk management, and ESG is a risk management tool, the board should approve the ESG strategy and supervise its implementation. It should also review the ESG disclosure by following a process similar to financial disclosure. However, to properly comply with their duties, board members need some basic understanding, and literacy, on ESG, and relevant training is an increasing concern.

Identifying which corporate area or department should coordinate ESG efforts within the company is important, and there is no one-size-fits all solution. The industry, whether it is heavily regulated or not, the maturity level of its functions and compliance systems, the regions where it operates, etc., are all relevant factors for a company to consider. In the past few years, the most common arrangement has been to entrust the Chief Sustainability Officer with this responsibility, although in-house lawyers and compliance officers are playing a more prominent role as a response to the increased attention of authorities to ESG matters. Governance is the basis of any effective ESG program and legal counsel typically oversee governance matters.

Deciding on which reporting framework to use is another factor. The multiplicity of frameworks and criteria, as well as the lack of standardization among them, are widely recognized as shortcomings of ESG. Although progress has been made for convergence at the global level, there is still much work to be done. If the company is not legally or contractually obligated to follow a specific framework, it is useful to inquire which ones are most common in its industry. Companies sometimes use a combination of two or more.

Identifying the right sources is also a common challenge. ESG is under development and can be a very broad concept; therefore, it is not easy to tell where it starts and ends. Companies need to identify the material obligations under domestic laws and regulations concerning environmental, social and governance matters. However, they should also track the public commitments (e.g., net zero by a certain date), contractual obligations and any requirements provided by foreign laws and regulations that apply to subsidiaries or vendors that are part of the supply chain. Additionally, companies should be aware of evolving industry standards and best practices.

Finally, developing a robust ESG compliance system is difficult. The right strategy, structure, policies and procedures, KPIs and controls for tracking, monitoring and reporting requires time and effort. Moreover, since ESG is a discipline under construction, the system requires constant fine-tuning and testing. A reliable system is critical for a strong ESG strategy.

12. What information sources are most relevant for ESG considerations in Mexico?

ESG in Mexico is still developing, and local sources of information for ESG matters are limited. Certain entities are currently engaging in efforts to make ESG information available. For example, “MexiCO₂”, a BMV sponsored platform that works on the development of environmental markets for Mexico’s transition to a low-carbon economy by helping companies and organizations identifying opportunities and structuring green projects. MexiCO₂ was created in 2014 with the support of the Ministry of Environment and Natural Resources (SEMARNAT), the Embassy of the United Kingdom in Mexico, the National Institute of Ecology and Climate Change (INECC), the National Forestry Commission (CONAFOR) and the United Nations Environment Programme (UNEP).

Additionally, the ESG Index, launched in 2020 by the BMV jointly with Standard & Poor’s, provides information on listed companies that successfully operate with ESG criteria. Currently, this ESG Index is comprised of 29 companies from different sectors. In the words of BMV’s top management, “the ESG Index has become the most aspirational index” for Mexican public companies. Also, in February 2023, BIVA launched “BIVASG”, an information distribution tool that provides relevant and up-to-date information on methodologies, regulatory changes, and securities transactions, as well as ESG-related information of registered issuers in Mexico.

Moreover, the Mexican Council for Sustainable Finance regularly publishes relevant information regarding ESG-related financing, especially information related to the issuance of green and other types of sustainable bonds in Mexico.

13. Has Mexico developed a Taxonomy related to ESG?

There is no taxonomy related to ESG in Mexico. However, as noted in response to Question 7, in early 2022 the Mexican Association of Retirement Funds Managers (AMAFORE) announced it was working on an ESG taxonomy, which was expected to be completed and released in 2022. Even though the taxonomy has not been released, participants of the private and public sector continue engaged in the drafting and approval process.

Such taxonomy is set to apply to Mexican retirement fund managers (AFOREs) and investment companies specialized in retirement funds (SIEFOREs) and will provide guidelines to these entities regarding the selection of investment projects based on ESG criteria and to avoid greenwashing. Despite the taxonomy’s limited application to retirement fund managers only, it is expected to serve as a precedent for the discussion of wider ESG-related taxonomies for the Mexican market.

Moreover, several AFORES convened and coordinated by the AMAFORE, have drafted and approved a unified questionnaire that will be shared soon with companies listed in Mexico so that the AFOREs can obtain consistent information and simplify the process for the responding companies. This questionnaire contains 217 questions, including 46 environmental-related questions, 103 social-related questions and 68 governance-related questions.

14. What does the future hold for ESG in Mexico?

ESG is in its early stages in the Mexican market, as compared to other jurisdictions. However, it is safe to predict that the relevance of ESG will continue to grow.

Although ESG has received attention from the Mexican financial authorities, market forces will continue to be the primary driver of change. Both Mexican authorities and market participants will continue to pay close attention to regulatory developments in the European Union and the U.S. for the development of domestic regulation.

Mexico is one of the countries with the highest number of international trade treaties, which makes it a very open economy. International trade, the increasing presence of global institutional investors and the international standards used by financing entities will continue to raise the bar on ESG matters for participants in the Mexican market.

We anticipate that topics such as climate change and environmental protection, anti-corruption and labor and working conditions will remain high on Mexico's agenda.

One particular feature of the Mexican ESG landscape is the role of the Mexican government as a driving force. For example, Mexico's government has been one of the largest and most successful issuers of ESG-themed bonds, which combine energy, environmental and infrastructure goals with social advancement causes.

Additionally, in 2018 the General Law on Climate Change was reformed to include (among other things) an obligation for the Mexican government to create an Emissions Trading System (ETS) to support the development of clean energy projects. Further, the government also supports the current implementation of voluntary carbon offsets with the participation of multiple private stakeholders, mainly through standard verification processes such as Verra or Gold Standard.

The implementation of an ETS and voluntary carbon markets is one of the Mexican government's solutions to achieve the goals of the Paris Agreement. Currently, the ETS is in a test stage: the only participants are facilities that carry out activities in the energy and industry sectors with annual emissions equal to or greater than 100,000 tons of direct carbon dioxide emissions. It is expected that the ETS will become generally operative in 2023.

It is safe to predict that in the coming years, the framework of hard and soft law regarding ESG-related matters will continue to grow in Mexico. This will lead to more companies implementing and adopting ESG strategies and criteria in their operations and day-to-day business.

We expect ESG activism to rise in Mexico, yet differently from the U.S. or the UK. Most (if not all) Mexican public companies have controlling shareholders or groups, so public campaigns by activist shareholders are less effective and,

therefore, uncommon. Institutional investors typically have conversations regarding ESG-related matters (including questions or concerns) with the investor relations department, rather than with companies' top management (e.g., CEO, CFO, CSO) or board members. We expect that these global and domestic institutional investors (investment funds, insurance funds and pension funds) will continue to push Mexican companies to further incorporate ESG-related metrics into their operations and disclosure documents.

Moreover, social activism by local leaders and communities will continue to play a key role in shaping the ESG landscape, especially regarding water availability, pollution and other forms of environmental and social impact.

All the above means that the bar will be raised for managers and directors of Mexican companies, and their roles will become more complex and demanding.

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Luis is a partner of Von Wobeser y Sierra. He has more than 30 years of experience in M&A and corporate matters and transactions in general. He is a member of the firm's Executive Committee, co-leads our Energy and Natural Resources industry group and is part of the ESG practice group. He has a diverse corporate practice with a focus on mergers and acquisitions and corporate and commercial transactions in general. This includes spin-offs, strategic alliances and information and communications technology (ICT) transactions, both domestic and cross-border, with an emphasis on the consumer goods, energy and technology sectors.

His clients include public companies listed in the Dow Jones, S&P, DAX, Nikkei and BMV, some of the most profitable Forbes 100 Top Brands, as well as some of the largest and most innovative private equity and venture capital funds. He has been a key player in the most groundbreaking and complex M&A matters and transactions that have recently taken place in Mexico and Latin America.



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Prior to joining Von Wobeser y Sierra, Pablo was the Global Vice President of Reputation and Communications at Anheuser-Busch InBev (AB InBev), the world's leading brewer, based in New York City. His previous position at AB InBev was Vice President of Legal and Corporate Affairs for Grupo Modelo and the Middle Americas zone, where he was responsible for the legal function, as well as the company's public affairs, including corporate reputation, communications, crisis management and social responsibility.

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NETHERLANDS

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This chapter forms part of:

ENVIRONMENTAL, SOCIAL & GOVERNANCE
Law Over Borders Comparative Guide 2023

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1. How is “ESG” in the Netherlands defined in a corporate/commercial context, and what are its major elements?

In recent years ESG has evolved from being, predominantly, a topic of (corporate) public regulation, to being part of the broader commercial and corporate law topic of ‘sustainability’. Moreover, soft law notions relating to ESG, which are voluntarily adhered to by corporates, are rapidly evolving into sources used to develop binding legislation, fill open legal norms and shape legal obligations. This trend, with additional emerging legislation and societal pressure, has caused ESG and sustainability to become board issues.

As a result of the emerging reporting obligations on a variety of ESG topics and the legislation applicable to a broad range of companies, there is growing focus on ESG as an integral part of a company’s strategy. Conducting business in a sustainable manner has become a prerequisite for access to investments, attracting new talent, and managing reputational matters.

In the Netherlands, there is no particular emphasis on a specific area of ESG in the sense that all components, in principle, require the same priority. Two topics, however, are worth separately mentioning:

- climate change, this is considered one of the most urgent topics impacting all ESG aspects; and
- nitrogen emissions, a 2019 ruling by the highest administrative court continues to impact all construction, industry and infrastructure projects in the Netherlands.

2. What, if any, are the major laws/regulations in the Netherlands specifically related to ESG?

ESG is a broad theme that encompasses a wide range of regulation. ESG-related matters are regulated through general rules of law as well as through specific legislation.

In the Netherlands, the **general** standard of tort is of importance as it has historically been used as a basis for civil redress for environmental protection. Generally speaking, open norms have been used to shape ESG-obligations.

In addition, existing legislation is in place for **specific areas within the sphere of ESG**, as follows:

- Focusing on the “E”, environmental protection is mainly regulated through the Environmental Management Act, the Nature Conservation Act, the Soil Protection Act and, by the Environment Act, which is expected to enter into force on 1 January 2024. In general, a company has a duty of care to refrain from performing an activity which results in significant adverse consequences for the physical environment, or if such consequences threaten to arise from it. Separately, in light of growing concerns regarding climate change, the Climate Act sets reduction targets of greenhouse gas emissions in the Netherlands by 2030 and 2050.
- Focusing on the “S”, relevant acts are the Equal Treatment Act and the Diversity Act. The Diversity Act (2022) introduced a quota for the supervisory boards of Dutch Amsterdam-listed companies as well as gender balance targets for the board and senior management levels of “large” listed and non-listed Dutch companies.

- As for the “G”, the Corporate Governance Code stipulates *inter alia* that management boards have a fiduciary duty to consider the environmental and societal impact of the company’s strategy. As of the financial year starting on or after 1 January 2023, the Code emphasises ESG and defines long-term value creation, as “sustainable long-term value creation”. In sum, the “G” covers business ethics, business conduct, values and corporate culture. These factors underpin the capacity of the company to include and consider environmental goals and social standards.
- Focussing on **disclosure regulations** in the Netherlands, the Civil Code requires large companies to include a statement on non-financial performance indicators in the board’s statement within the annual report (Articles 2:391 and 2:397 Civil Code). Such stipulations are the consequence of EU law, specifically the EU Directive 2014/95 regarding disclosure of non-financial and diversity information by certain large undertakings and groups) (NFRD). In January 2023, the Corporate Sustainability Reporting Directive (CSRD) entered into force. The CSRD, through 12 underlying Sustainability Reporting Standards (ESRS), imposes detailed sustainability reporting requirements at EU level on a large group of companies covering a wide variety of sustainability related topics, including ESG matters, respect for human rights, anti-corruption, and anti-bribery. It will significantly change and expand the ESG disclosure landscape in the Netherlands.
- Furthermore, **due diligence obligations** are likely to increase. The Child Labour Due Diligence Act was enacted in 2019, but has not yet entered into force. Furthermore, a draft initiative bill on Responsible and Sustainable International Business Conduct (“Initiative Bill”) is pending in Parliament, obliging all Dutch undertakings operating internationally to take every possible measure in order to prevent, mitigate and limit adverse effects on human rights, labour rights and/or the environment of their activities. The Dutch government initially planned to develop a separate Dutch Act on Corporate Social Responsibility, but the Minister for Foreign Trade and Development Cooperation recently reported that this plan is not (yet) being rolled out in view of the initiative bill. The minister is, together with the drafters of the bill, exploring options for a bill that would receive broad support. The bill however received significant criticism. In parallel, on an EU level, a proposal for a Corporate Sustainability Due Diligence Directive (CSDDD) was published, with the aim to directly regulate corporate social governance in general instead of only indirectly via the non-financial reporting obligations of the NFRD. Direct regulation through mandatory due diligence of supply chains, nevertheless, does exist for specific high-risk sectors such as timber or conflict minerals. The CSDDD proposal introduces a substantive corporate duty for certain companies to perform due diligence to identify, prevent, mitigate and account for external harm resulting from adverse human rights and environmental impacts in the company’s own operations, its subsidiaries and in the value chain. Other proposals containing due diligence stipulations pending at EU level are, for example, laid down in the draft Deforestation Regulation (2021/0366(COD)), the new Batteries Regulation (2020/0353(COD)) and in the Proposal by the Commission prohibiting the placing on the EU market of products made by forced labour (COM/2022/453 final).

3. What other laws/regulations in the Netherlands touch on ESG themes?

In this respect, there are several initiatives to highlight:

- The Netherlands has anti-money laundering regulations in place. The most important act is the Money Laundering and Terrorist Financing Prevention Act, implementing EU law (Anti-Money laundering Directives).
- In 2020/2021 the Dutch Competition Authority (ACM) published in 2020/2021 its Draft Guidelines on Sustainability Agreements. By doing so, the ACM acknowledges that collaboration between corporates can positively contribute to the achievement of public sustainability goals. In order to combat greenwashing and provide some guidance in this respect, in January 2021, the ACM published Guidelines on sustainability claims, which provide a set of five rules of thumb for businesses in making and phrasing sustainability claims. The ACM increasingly actively enforces these guidelines through dialogue and, if needed, enforcement of behavioural remedies or fines. In addition, the Dutch Advertising Code Committee (Reclame Code Commissie) tightened the rules for sustainability claims in advertising.
- ESG plays an important role in public procurement regulation. The Public Procurement Act expressly sets environmental thresholds on energy for public buyers. Furthermore, the central and decentralised governments have concluded a Manifesto for Socially Responsible Contracting and Procurement, according to which governments concerned must take into account impacts on environment and biodiversity, climate, circular (including bio-based), International Social Conditions (chain responsibility), diversity and inclusion and social return.

4. What, if any, litigation or enforcement activity has the Netherlands seen related to ESG?

ESG-related issues have been the subject of a wide range of litigation in the Netherlands:

- Sustainability claims in advertising have been challenged before the Advertising Code Committee. The rulings frequently create much publicity. The same applies to the regulation of sustainability claims pursuant to the Guidelines on Sustainability Claims by the ACM, as discussed in the previous section.
- Public enforcement cases are numerous. They range from filing objections against permits, requests to revoke licenses, as well as enforcement requests to public authorities. The highest administrative court has ruled more than once that national legislation was contrary to the Habitats Directive, having far-reaching consequences for the industry and all infrastructure and construction projects and also led to numerous enforcement requests against airports, industrial sites and farms. More recently, NGOs in the Netherlands have requested that the Dutch Financial Markets Authority (AFM) enforce ESG disclosure obligations. For example, NGOs may find that a specific company has not made some or all required ESG disclosures and ask the AFM to enforce compliance in respect of that specific company.

- As in other jurisdictions, private enforcement in the Netherlands is on the rise. Examples are:
 - The *Urgenda*-case (Supreme Court, 2019) and the *Friends of the Earth Netherlands et al. v. Royal Dutch Shell* judgment (first instance, 2021, under appeal). Both cases concern fighting climate change and decreasing carbon emissions.
 - Several private enforcement actions against airports, aviation companies and the Dutch State concerning CO₂ emissions and the obligation to reduce CO₂ emissions are currently pending.
 - Enforcement actions on the basis of unfair trade practices or general tort law are also pending. An example is a case filed by an NGO against an aviation company. According to the campaigners the aviation company breaches European consumer law by misleading advertisement claims.

We expect public and private enforcement to increase in coming years in view of funding initiatives as well as on the basis of imminent European regulations.

5. What are the major non-law/regulatory drivers of ESG trends and developments in the Netherlands?

Soft law instruments

In the Netherlands, there is not necessarily a strict separation between the various binding regulations and soft-law instruments. Notions of soft law may, depending on their precise content and the issue at hand, be one of the factors informing the interpretation of open legal norms. For example, in its May 2021 *Shell* ruling in first instance (subject to appeal), The Hague District Court found that in determining what the unwritten standard of care required under general Dutch tort law is, the United Nations Guiding Principles on Business and Human Rights (UNGP) are suitable as guidelines regardless of whether the defendant company involved has committed to the UNGPs because, according to the court, their content is “universally endorsed”.

The ambition to confirm and supplement the most important aspects of the Organisation for Economic Co-operation and Development (OECD) Guidelines, such as the recommendations regarding due diligence obligations into binding legislation is however clearly visible both on the EU level, as well as on the national level.

The International Corporate Social Responsibility (CSR) policy has been based on voluntary measures via the stimulation of sectoral cooperation through covenants. After an evaluation the Dutch government announced it would await EU legislation given the importance of having a level playing field across the EU. The Dutch government has already developed a new policy for state participants requiring them to set ambitious targets on climate, environment, a safe working environment, human rights, financial transparency, and anti-corruption, to be tested periodically. As for its efforts regarding the private sector, the government updated its National Action Plan Business and Human Rights, focussing on realising the UNGPs within the three pillars, one of which is the corporate responsibility to respect human rights.

Moreover, a development we expect that pledges, endorsements, and other similar instruments will play a more prominent role in litigation on how to interpret and apply open norms and/or assess behaviour in the context of unfair market practices.

Stakeholders

ESG is currently on the agenda at the level of Members of Parliament (MPs), government, regulators, NGO's, corporates, stakeholders, as well as investors.

Regulators such as the ACM as well as the Dutch Financial Supervisory Authorities, AFM and the Dutch Central Bank (DNB), have developed guidelines on sustainable investment, horizontal cooperation and greenwashing.

Nevertheless, in the short term, climate litigation by NGOs and mass claims (both supported by litigation funders) are expected to be a large driving force in ESG trends. Most notably in this context are the aforementioned *Shell* and *Urgenda* rulings. In 2022, Friends of the Earth summoned various Dutch multinationals to reduce emissions and announced it will start new similar proceedings if necessary. Furthermore, in 2020, the so-called WAMCA act entered into force. This act clears the way for collective actions for damages, which is expected to spur ESG-related litigation, and funding thereof.

Investor representative organisations are also engaged in ESG. Eumedion, for example, is a representative body of institutional investors in Dutch-listed companies. For 2023, Eumedion's focus points are the implementation of the CSRD and the European Sustainability Reporting Standards, the effectiveness and improvement of say-on-pay legislation, and the proposed legislation on due diligence. In addition, Eumedion requested companies in their Focus Letter 2023 to take actions on the dependencies and impact of the company related to biodiversity and to be transparent about human rights strategies. Certain private equity firms – in turn also pushed by their limited partners – apply similar pressure on their portfolio companies, requiring them to adopt and provide transparent disclosure on their ESG strategy and the implementation thereof. The same goes for banks and other financial institutions: their own shareholders as well as their regulators require banks to disclose on their ESG footprint, which increases the focus on the position of their clients.

National Contact Points (NCPs)

The Dutch NCP deals primarily with specific instances of alleged non-observance of the OECD Guidelines and facilitating dialogue. This concerns a wide range of matters such as funding, engagement by institutional investors and social aspects in portfolio companies. From the NCP's yearly report, it is clear that their focus is on about a dozen cases per year. As of 2014, the NCP was endorsed by the Dutch government to also conduct cross-company research.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

Although ESG disclosures are an important aspect of ESG-regulation in general, it is not the dominant topic as is discussed in Question 2. Due diligence obligations

are an important part of the regulation plans of both the Dutch as well as the EU legislature. The proposed regulatory frameworks will make the so-called ‘six OECD steps of due diligence’ mandatory. Initiatives include civil liability. Furthermore, companies are required to draw up climate plans to reduce emissions and work with climate scenarios, which means having a climate policy in addition to a disclosure obligation.

As mentioned in Question 2, disclosure regulations in the Netherlands are based on EU law. This includes the NFRD, the Regulation on sustainability-related disclosures in the financial services sector (SFDR), the Taxonomy Regulation for Sustainable Activities (Taxonomy Regulation), and the Regulation on prudential requirements for credit institutions (Capital Requirements Regulation).

In general, ESG disclosures must – except for the SFDR disclosures – be included in the board’s statement in the annual report on nonfinancial performance indicators. SFDR disclosures are – depending on the activity and period in time – required to be published on institutions’ websites, as pre-contractual disclosures, and in the form of periodic reports.

In general, ESG disclosures in the Netherlands are required on an annual reporting basis. The SFDR also requires ESG disclosures prior to investments and on a more continuous basis.

As for standards, when the CSRD comes into effect, all large companies and all listed companies will be required to report on ESG aspects (double materiality) in the management report on the basis of ESRS. As for companies voluntarily expanding their disclosures on ESG-related issues, these often refer to the standards of the Global Reporting Initiative (GRI) and the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD), and report on their operations and policies. Specific sectors have also formalised voluntary additional reporting.

7. Which sectors are most impacted by ESG in the Netherlands? How significant is ESG investment in the Netherlands?

As a consequence of the EU Green Deal and the transition towards a sustainable society, many legislative initiatives are being taken at EU level. These initiatives impact all sectors. This is, for example, the case with the Fit for 55 Package legislation of the European Commission.

An important sector to which regulation is directed is the financial sector. The European Commission designated the financial sector as one of the driving forces of “mobilising capital” towards a sustainable market. The most significant ESG investments are therefore made in the Netherlands by financial institutions as part of their sustainability strategy and regulatory obligations.

In addition to large public interest companies that were already in scope of certain sustainability disclosure obligations, small and medium enterprises (SMEs) will incur significant effects as well. Large public-interest entities (PIEs), such as listed companies, banks, and insurers are relatively less impacted by the new CSRD disclosure obligations (as mentioned under question 2) compared to listed SMEs. PIEs were already under ESG disclosing obligations due to the NFRD. The CSRD brings listed SMEs under the scope of ESG reporting. The CSRD also

imposes major new and extensive sustainability disclosure obligations on large PIEs: companies are required to provide information about their strategy, targets, the role of the board and management, the principal adverse impacts connected to the company and its value chain, intangibles and how they have identified the information they report. This information needs to be reported on the basis of the ESRS. The European Commission will ultimately have to adopt the final ESRS, and implementation in the Netherlands is expected to occur through an executive order that is intended to be enabled on the basis of the Act implementing the Directive on disclosure of income tax information.

As for ESG due diligence obligations, the CSDDD will not formally apply to the vast majority of EU companies. About 99% of the companies can be classified as small and medium-sized enterprises, and are therefore exempt from the CSDDD. The Commission has estimated that about 13,000 EU companies will fall under the scope (and 4,000 third-country companies). The exempted companies will, however, be indirectly affected through their business relationships with the companies that do fall under the scope of the CSDDD, since these companies will need to provide information to companies in scope in order for them to effectively meet their due diligence obligations. However, for companies that may indirectly be affected by the CSDDD proposal, a Guideline was published by the European Commission which contains guidance on designing effective and inclusive accompanying support to due diligence legislation as well as information on portals, websites, and so on. Also, certain so-called high-risk sectors will be impacted if the draft CSDDD is adopted. On that basis, the EU will, under certain conditions, impose mandatory due diligence requirements on high-risk sectors such as textile, fishery, agriculture, forestry, and mineral extracting sectors.

Furthermore, we note that some companies merely follow legislation while others add to this by taking initiatives on their own account.

Private equity

Private equity covers a myriad of sectors and companies where each has their own ESG aspects to consider. Private equity firms, on the one hand, can have the opportunity to invest in businesses divested by companies that are subjected to more stringent ESG-regulation. On the other hand, private equity firms can apply pressure on their portfolio companies, requiring them to adopt and provide transparent disclosure on their ESG strategy and the implementation thereof. The same goes for banks and other financial institutions: their own shareholders as well as regulators and European regulations require banks to disclose their ESG footprint, which increased the focus on the position of their clients.

Banks and other financial institutions

We see that sustainability initiatives have, to a large extent, become an integral part of banks' business strategies. Financial institutions in general are designated by the EU as major drivers in the transformation towards sustainable markets. For example, the SFDR specifically covers the financial sector. This is advanced through several means, such as scrutiny of institutions' own risks in their portfolio

as part of prudential regulation, mandatory disclosures of sustainability features of products, and requirements to articulate sustainability considerations in their investment policies.

Voluntary initiatives are a key part of the financial sector's contribution to sustainability.

Fashion

The CSDDD, the Child Labour Due Diligence Act and OECD guidelines are, and will continue to be, increasingly relevant for the fashion sector because their supply and value chains are under intense scrutiny regarding working conditions and child labour. Moreover, the fashion industry is clearly in scope of the ACM's efforts to enforce its Guidelines on sustainability claims as recent cases against Decathlon and H&M show.

Energy industry

The energy industry is highly impacted by the broad context of ESG in the context of climate change and emissions as well as through its role in the energy transition. The transition towards renewable energy and the reduction of emissions is an immense challenge. The transition to net zero and climate change causes new ESG challenges as is, for example, shown by the discussion on the adverse impact of lithium on local communities and the environment.

By way of example, the Dutch transmission system operator, has drawn up a so-called 'Green Bonds Framework', which serves as a framework for monitoring the sustainability quality of the projects financed by issuing green financing instruments and is one of the largest issuers of Green Bonds in the world.

Real estate industry

The real estate industry is likely to become highly impacted in the Netherlands. First, the physical risk of climate change could be significant in the Netherlands and may seriously affect living environments. In addition, ESG concerns will have an effect on pricing by, and the requirements from, investors and debt providers with respect to the real estate industry. ESG data management and reporting will significantly enhance the capabilities of pricing in climate risk in the real estate industry.

8. What are the trends in the Netherlands regarding ESG governance?

Governance of ESG differs between companies. The structure of the ESG governance depends on, for example, the sector in which the company operates and the level of ESG maturity within the company. ESG-related matters are often covered by one project team within the organisation, but ESG can also be integrated in the existing organisation or covered by dedicated ESG functions throughout the organisation.

There is a clear trend that ESG has become a board issue and also the governance of ESG is of greater interest of stakeholders and other parties. This is emphasized by the mentioned update of the Corporate Governance Code, stipulating that

boards have a fiduciary duty to consider the environmental and societal impact of the company's strategy.

Further, we expect the CSRD will have a significant impact on sustainability reporting in the Netherlands, both in terms of scope and in terms of nature. These disclosure obligations will result in greater scrutiny towards companies, as well as the companies' governance over ESG, from regulators, supervisory authorities, and consumers. We expect the AFM to increase its focus on ESG disclosures and the ACM and consumers to intensify their focus on greenwashing (see Question 4). Furthermore, we see that companies are increasingly focused on climate scenario planning and establishing a framework to assess the resilience of a company in all uncertain yet possible climate scenarios.

Lastly, we envisage that further clarifications will be needed on, for example, assurances by auditors with respect to sustainability disclosures and other technicalities concerning the role of auditors.

9. To what extent are ESG ratings or ESG benchmarks relied upon in the Netherlands?

ESG rating agencies

Currently, there are no formal requirements regarding governance of ESG service and product providers. Consequently, users cannot always trust the presence of certain quality and reliability safeguards. The AFM has recently stated to be in favour of specific requirements on internal control and governance to ensure reliability and quality of the services provided, as well as proper management of conflict of interest. The latter can arise from the different roles these providers can have.

ESG benchmarks

Most companies include ESG benchmarks on their websites or in publications. The AFM has stated to be in favour of EU regulation for, among others, reasons of transparency concerning methodologies and underlying data of ESG ratings as well as for specific requirements in terms of governance and management of conflicts of interest. The CSRD and ESRS will create benchmarks to a certain extent, but will not solve the problem of assembling trustworthy ESG data, which are crucial for reporting.

10. What is the role of the private markets versus public markets in driving ESG developments in the Netherlands?

Private companies

Historically, in Europe, ESG regulation used to apply mainly to regulated markets (i.e. most significantly listed companies). Future ESG legislation will increasingly be directed towards private companies. For example, the CSRD will also be applicable to large private companies and, in subsequent years, to SMEs. The legislative proposals moreover explicitly allow for private enforcement of ESG regulation, on the basis of which increased market vigilance and litigation can be expected. At the same time, we observe that the market proactively makes use of

the Draft Guidelines on Sustainability Agreements by the ACM, which facilitate collaboration between corporates that positively contributes to the achievement of public sustainability goals.

Public companies

As set out in Question 7, PIEs have a broader variety of ESG reporting obligations when the CSRD proposal enters into force insofar as PIEs are driving ESG developments in the Netherlands. However, risks of greenwashing may be actual. We also observe instances in which less sustainable parts of the entities' activities are being divested to private companies resulting in not having to disclose on these activities. As also described in Question 7, the CSRD, when adopted in its current form, will bring listed SMEs in due time under the scope of mandatory ESG reporting.

Government-owned organisations

Government-owned entities should take leadership on ESG issues according to the new policy document. The government expects these entities to set an example in their own sectors in pursuing a positive impact on people, society and the climate. The level of ambition of these entities of CSR is periodically assessed.

ESG agenda

See above, Questions 4 and 5.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

The most pressing challenge for companies will be the time frame within which companies will have to prepare for EU legislation. Large listed companies will need to disclose on the extensive CSRD requirements for the financial year 2024, meaning that the relevant, trustworthy data should be available by early 2025 at the latest. Obtaining trustworthy data and providing for sufficient safeguards in this respect will be a challenge in itself, as is the case for the lack of prioritisation under the CSRD.

Furthermore, companies will have to set up a due diligence framework under the CSDDD within a relatively short time while the scope and extent of the due diligence obligations under the proposed CSDDD are currently unclear.

Another difficulty around compliance will be the (perceived or actual) tension between companies wanting to set ambitious ESG-targets, while not meaning to be held liable in case these targets and ambitions are not met. On the other hand, companies setting less ambitious targets risk being held in breach of (perceived or actual) obligations to pursue more ambitious policies.

12. What information sources are most relevant for ESG considerations in the Netherlands?

First, ESG data is only available in a fragmented manner, and, in most cases, incomparable. Another concern is that ESG data tends to be limited or missing context (e.g. reporting high emissions in isolation often lacks context around the

products produced with these emissions while these products may in themselves serve the energy transition or transformation to a net zero economy).

In *Urgenda*, the Court ruled that, when interpreting the positive obligation of the Dutch State, account must be taken of widely accepted insights in science and internationally accepted standards. Moreover, the Court called the reports of the Intergovernmental Panel on Climate Change (IPCC) important in this regard and used these reports in its assessment.

Several other sources are used regularly by market players to assess their ESG performance. Widely accepted standards include the Science-Based Targets of the Science-Based Initiative (SBTi). Companies have joined the initiative to set science-based climate targets. Companies also rely on information of Morningstar Sustainalytics, which is an independent ESG and corporate governance research, ratings and analytics firm.

Finally, the EU is currently working on the creation of a European Single Access Point (ESAP) to ensure that investors have easy access to public financial and sustainability-related information on EU companies and EU investment products who make tagged disclosures on this pursuant to the CSRD.

13. Has the Netherlands developed a Taxonomy related to ESG?

The Netherlands has not developed a separate Taxonomy related to ESG since the EU Taxonomy Regulation is directly applicable in the Netherlands. The Taxonomy Regulation entered into force on 12 July 2020 and is a classification system establishing a list of environmentally sustainable economic activities. Alongside the SFDR, the NFRD and the proposed CSRD, the Taxonomy Regulation complements the sustainable finance regulatory regime. At the core of the Taxonomy Regulation is the definition of a sustainable economic activity. The EU Taxonomy provides for a 'green' taxonomy and a social taxonomy (see European Union chapter).

14. What does the future hold for ESG in the Netherlands?

In the short term:

- Development of legislation in relation to companies and ESG, including disclosures, is ongoing at the EU as well as at the national level. The first development has already been set into motion with the entry into force of the EU Taxonomy Regulation. As a consequence, all annual reports by relevant organisations published after 1 January 2022, must contain the information required by the Regulation.
- Due to the 2022 Russian invasion of Ukraine, the obligations for corporates active in the EU with respect to human rights due diligence in armed conflict has become topical. The UNGPs ask companies to develop a conflict-sensitive approach to mitigate and address human rights risks in armed conflict.
- Furthermore, we envisage increased monitoring by regulators and supervisory authorities. It remains to be seen whether supervisory authorities will be sufficiently equipped to carry out supervision properly and coherently. We expect the AFM to increase its focus on ESG disclosures and the ACM to intensify its focus on greenwashing.

- The social component of ESG is receiving increased attention, for example on the fundamental issue of equal treatment, in light of various societal developments related to gender and sexual orientation and diversity. These developments also extend to claims and litigation. For example, in 2020, Bureau Clara Wichmann, an NGO, initiated an action leading to compensation from the State for transgender persons suffering from mandatory sterilisation in the past and initiated proceedings to have free birth control provided to young women.

In the medium term:

- Substantively, the challenge of effectively addressing climate change is the subject of the current debate and legislative initiatives. As is evident from, for example, the European Commission's Fit for 55 package, this is an area where large parts of society will see significant changes in the short term but also in the next few decades. As for effects in the short term, we'd like to highlight that in December 2022, a provisional agreement was reached in the EU on the Carbon Border Adjustment Mechanism. As an example of the short term effect on the national level, we note that as of January 2023, the Minimum Carbon Price Act has entered into force, which aims at further taxing high-carbon-emitting industries, which are complementary to the current CO2 levy.
- In order to comply with the due diligence obligations for value chains, we expect that contracts within value chains may have to be renegotiated and that the structural reliance within value chains may therefore change. It may be further developed in case law, under which circumstances, ESG considerations could give ground to contractual amendments and/or termination rights.
- In addition, a general trend appears to be the expansion of the scope of stakeholders of companies that can rely on a certain duty of care and/or active due diligence and prevention of harm by these companies. We expect the focus of companies' performance in the medium term to shift from a predominant focus on financial performance to overall societal performance. This will also impact the duties of executive and nonexecutive boards, their function towards the company, and society at large.
- We expect more public enforcement on ESG, not only by AFM and DNB but also by other public authorities, due to pressure from NGOs and public scrutiny. This may pertain to greenwashing in general and to incorrect disclosures specifically.

- We expect the markets of ESG data rating companies and agencies to become regulated on EU level in order to ensure the transition towards a more sustainable economy.
- It is yet to be seen whether the emerging ESG-regulation will lead to asset partitioning and further protectionism.

In the long term:

- Investment will be geared towards sustainable initiatives. We expect that rising prices will cause countries to adopt taxation policies to counterbalance any impacts of the competitive advantage of unsustainable products.
- For multinationals domiciled in the EU and/or within scope of EU regulation, the challenge will be how to achieve an international level playing field and how to maintain their competitive position while meeting ESG/sustainability demands and complying with ESG regulation.

AUTHOR BIOGRAPHY



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Davine Roessingh is a partner in De Brauw's litigation and arbitration department and has extensive experience in litigation complex matters. She is co-head of De Brauw's ESG expertise group and highly knowledgeable on ESG regulation (including the impending CSRD, CSDDD and Ecodesign Regulation), and legal questions around decarbonisation and sustainability. She advises regularly on legal aspects of external communications on sustainability and due diligence obligations. Clients also seek Davine's advice in relation to ESG-governance, stakeholder engagement, climate scenario application, and board engagement. Together with the multi-disciplinary sustainability team of De Brauw, the advice rendered takes into account the multi-jurisdictional and complex spectrum of sustainability regulation. Davine also regularly lectures boards and legal departments on ESG-regulation upon specific requests of clients.

PERU

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Claudio Ferrero & Tomás Denegri
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This chapter forms part of:

ENVIRONMENTAL, SOCIAL & GOVERNANCE
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1. How is “ESG” in Peru defined in a corporate/commercial context, and what are its major elements?

There is no legal definition of “ESG” in the Peruvian legal framework. Therefore, when used in a corporate/commercial context, companies must incorporate the definitions of soft non-binding laws issued by international organizations (mainly, the United Nations). However, even though the concept of ESG has not yet been legally defined, it has been implicitly incorporated in certain laws and regulations approved for different economic sectors. Such laws and regulations focus on the disclosure and provision of information on issues related to social corporate responsibility, community relationship matters and sustainable development, among others.

2. What, if any, are the major laws/regulations in Peru specifically related to ESG?

ESG matters have not been regulated in a single unified text. However, the importance of ESG issues has been recognized by legal dispositions scattered in the regulations of different economic sectors. Thus, probably the most important are:

- **Supreme Decree No. 052-2010-EM**, which establishes that mining titleholders have to submit an Annual Affidavit containing information about the sustainable development activities executed by them during the previous year. The information provided in the Annual Affidavit covers the following matters:
 - education;
 - health;
 - nutrition;
 - local employment; and
 - basic infrastructure, among others.
- **Supreme Decree No. 019-2009-MINAM**, which regulates the National System of Environmental Impact Management. According to said regulation, titleholders of investment projects which generate environmental impacts must obtain the approval of an environmental management instrument prior to the execution of its activities. The procedure to obtain the approval of an environmental management instrument has a public participatory nature, in which stakeholders disclose information about the project, its potential impacts, as well as the environmental management measures to be adopted in order to prevent any negative environmental impact. On the other hand, environmental management instruments include a “community relationship plan”. A community relationship plan aims at achieving a healthy coexistence between the titleholders of an investment project and its stakeholders during the different stages of the project. Such plans cover actions related to the disclosure of information regarding:
 - the development of the investment project;
 - the channels through which stakeholders can raise objections to the investment project;

- the code of conduct that must be complied by the titleholder of the investment project;
 - specific programs for hiring local labor and for the local development that will be implemented by the titleholder of the investment project.
- **Superintendent’s Resolution No. 018-2020-SMV/02** approves the Corporate Sustainability Report, whose purpose is to provide shareholders, investors, and other stakeholders with relevant and accurate information on the policies, standards and actions that issuers are implementing to ensure their sustainability in the long term. The information to be presented in this report refers to the actions and standards implemented by a company in relation to the impact of its operations on the environment and social development. Specifically, companies provide information on:
 - their environmental policy;
 - greenhouse gas emissions;
 - water and energy consumption;
 - solid waste generation;
 - relationship with their stakeholders;
 - labor rights;
 - human rights, and so on.

3. What other laws/regulations in Peru touch on ESG themes?

Peru has laws and regulations that tangentially regulate matters related to ESG themes.

For instance, the General Environmental Law (Law 28611) contains a general reference to the promotion of “social corporate responsibility”.

On the other hand, in recent years, due to corruption scandals that involved past Governments, new laws relating to corporate governance have been issued. These laws mainly regulate the criminal liability of corporations, their directors and managers, as well as anti-bribery and anti-money laundering.

4. What, if any, litigation or enforcement activity has Peru seen related to ESG?

There has been no litigation or enforcement activity in Peru directly related to ESG. However, in relation to advertising matters, there have been cases in which companies have been denounced or sanctioned for disclosing false or inaccurate information, or for not complying with the consumer protection standards issued by Peru’s National Consumer Protection Authority (INDECOPI). In fact, there are cases in which the inaccuracy of the information provided has been related to the fact that the products had ecological characteristics or were produced respecting the environment (greenwashing). Although advertising regulation is not directly related to ESG matters, it is a regulation that emphasizes the quality, quantity, type and accuracy of the information provided to consumers. For that reason, we mention it as an example, since it shows that when it comes to the disclosure of information, there have already been sanctions imposed by Peruvian regulators.

On the other hand, in the past few years, public prosecutors have been very active in investigating corruption scandals within a corporate and commercial context, which has forced Peruvian companies to adopt corporate measures to avoid criminal liability. The implementation of compliance programs and anti-bribery and anti-money laundering training is mandatory for certain industries, such as legal services, banking & finance, etc.

5. What are the major non-law/regulatory drivers of ESG trends and developments in Peru?

Probably, the main driver for the promotion and development of ESG regulation in the country is given by the weight that this kind of information has on investors. For them, this information is a key element when analysing and choosing one investment from another. Therefore, it is possible to point out that, eventually, the main trend in ESG regulation comes from the securities market.

However, another major driver for promoting ESG regulation comes from the mining sector. In fact, the mining industry is one of the pillars of the Peruvian economy and arguably the most important sector. It is extremely important to conduct mining activities with a social management strategy aiming to promote and seek the participation and inclusion of every stakeholder. It is for this reason that mining regulation, along with the securities market regulation, has been the pioneer in enacting legal dispositions related to ESG matters (see Question 2), for regulating the disclosure of information on how mining companies promote sustainable development.

Soft non-binding laws

It is common for Peruvian companies to include references to the UN Guiding Principles of Business and Human Rights, the OECD Guidelines for Multinational Enterprises and the ILO Convention on forced labor in their agreements.

Stakeholders

In addition to the mining sector, there are two groups which are particularly engaged in the promotion of ESG in Peru: local and international NGOs and financial institutions. International corporations are also very active in pushing a sustainable corporate agenda, but this is related to their corporate policies as an economic group, rather than a local initiative.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

Not all of the legal dispositions mentioned in Question 2 are related to the disclosure of information. In fact, in the case of mining regulation, the Annual Affidavit regulated by Supreme Decree No. 052-2010-EM does not have a public nature. Therefore, it contains data about sustainable development measures and investments that will only be disclosed to the Ministry of Energy and Mines.

Regarding Supreme Decree No. 019-2009-MINAM and the obligation of operating with a community relationship plan as part of the environmental management instrument, the actions contained in the community relationship plan are linked to corporate disclosure. Indeed, among others, community relationship plans encourage the disclosure of information about the development of an investment project in favor of its stakeholders.

Reporting

Since 2015, companies listed on the Lima Stock Exchange are obligated to submit yearly sustainability reports. The Corporate Sustainability Report, required to be submitted by all issuers with securities registered in the Public Registry of the Securities Market, is essentially comprised of information that will enable shareholders, investors and other stakeholders to have relevant and accurate information on the policies, standards and actions that issuers are implementing to ensure their long-term sustainability.

7. Which sectors are most impacted by ESG in Peru? How significant is ESG investment in Peru?

In our view, financial institutions, issuers with securities registered in the Public Registry of the Securities Market, mining, electricity and oil & gas companies are the economic sectors most impacted by ESG in Peru. These are subject to a heavy public scrutiny, which has led to a demand for mining and oil & gas companies to pursue a sustainable corporate agenda. Moreover, specific public participation regulations have been approved for mining, electricity and oil & gas companies (by means of Supreme Decree No. 002-2019-EM, Ministerial Resolution No. 223-2010-MEM/DM, and Supreme Decree No. 028-2008-EM, the Citizen Participation Regulations for oil & gas, electrical and mining activities, respectively, were approved) to:

- strengthen the stakeholders' rights of access to information and citizen participation;
- promote healthy relationships between the stakeholders, the State and the projects' titleholders; and,
- provide the environmental competent authorities with sufficient information to take decisions on the environmental and social management of the economic sectors mentioned above.

In the case of the mining sector, regulations have even been approved to disclose information before the Ministry of Energy and Mines on how mining companies promote sustainable development (i.e. Supreme Decree No. 052-2010-EM, see Question 2). Additionally, when submitting a mining pediment for obtaining the granting of a mining concession, titleholders have to sign an affidavit by means of which they declare that they will execute sustainable development actions when executing their activities.

8. What are the trends in Peru regarding ESG governance?

There have been some advances in Peru in terms of corporate compliance and governance, and the promotion of an ethical business culture, specifically in

connection with the implementation of compliance programs in organizations. In fact, in recent years, the regulations related to “crime prevention models” (Law No. 30424, Law that regulates corporate liability for corruption and money laundering offenses, and its Regulations) and to anti-money laundering and counter terrorism financing (AML/CFT regulations) require that top management bodies assume the duty to implement and supervise compliance programs.

For example, regulations of Law No. 30424, explicitly states that the highest government, administrative and senior management bodies of a legal entity or those acting on their behalf, are responsible for leading the implementation and adequate functioning of the prevention model, through their commitment and firm, active and visible support. This implies that these bodies have a leading responsibility in the appropriate execution and functioning of the compliance program and are accountable before the company.

In addition to this, Law No. 30424 and in AML/CFT regulations, designing a prevention officer or compliance officer by the company’s highest governing body is established as a minimum component of these systems. Unfortunately, there is still a belief that the role of the governing and administrative bodies begins and ends with this designation (and in the case of AML/CFT systems, that it would also end with the approval of the internal policies and relevant documents), which is inaccurate.

9. To what extent are ESG ratings or ESG benchmarks relied upon in Peru?

ESG rating agencies

The S&P/BVL Peru General ESG Index was launched by the Lima Stock Exchange (Bolsa de Valores de Lima) in November 2021. The Peruvian ESG Index was designed to reflect the performance of the companies listed in the S&P/BVL Peru General Index and that meet the environmental, social and governance criteria defined in S&P Global’s Corporate Sustainability Assessment. Currently, there are 15 companies that make part of the S&P/BVL Peru General ESG Index.

ESG benchmarks

The Lima Stock Exchange refers to S&P Global’s Corporate Sustainability Assessment.

10. What is the role of the private markets versus public markets in driving ESG developments in Peru?

Private companies

Private companies are, principally, integrating ESG issues into their business strategies by adhering to the principles and reporting frameworks of renowned NGOs (such as, the UN Global Compact, the Global Reporting Initiative, and, locally, Peru Sostenible) and by complying with the regulations (see Question 2) when applicable. This is in addition to the internal policies of the larger multinational economic groups to which Peruvian subsidiaries are also bound. For instance, internal corporate regulations governing the relationship that a certain company, its workers and suppliers or service providers must have with local communities.

Public companies

Public companies follow the same trend as private companies. In our view, there is no major difference between the role of private and public markets in respect of ESG requirements in Peru.

Government-owned organizations

Currently, ESG considerations are not key in government-owned organizations, or in organizations in which the government has a stake.

ESG agenda

Principally, the ESG agenda in Peru is pushed by private stakeholders, along with the work of NGO's (for example, the UN Global Compact or the Global Reporting Initiative) This ESG agenda is increasingly responsive to global trends.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

The Peruvian economy is mainly informal. Peru's main challenge in terms of compliance under ESG obligations is to start formalizing the economy. This will allow the Government to have a broader supervision of the different activities and obligations of the companies and facilitate the enforcement of ESG obligations.

The informal economy has resulted in limited data regarding the compliance of companies with their legal (environmental and social, for example) obligations, and is the main barrier to effective ESG measures in Peru.

As mentioned, there are a few legal disclosure obligations related to ESG matters in Peru. Consequently, other than those already described related to compliance, anti-bribery, anti-money laundering and anti-corruption laws, companies in Peru do not face any additional legal challenges in respect of compliance under ESG matters.

12. What information sources are most relevant for ESG considerations in Peru?

The most relevant information sources for ESG considerations in Peru are high profile NGOs. For example, Peru Sostenible is a corporate network whose purpose is to promote the UN's Sustainable Development Goals within Peru. Peru Sostenible gathers information on more than 80 companies within different economic sectors.

The Global Reporting Initiative is the main private measurement frameworks that companies are integrating into their business models in Peru.

Regarding the public sector, the Ministry of Environment has implemented the National Registry of Mitigation Measures (RENAMI, for its acronym in Spanish) which has the purpose of collecting, recording, monitoring and managing the information on the advances of the reduction of greenhouse gas emissions by means of the execution of mitigation measures, which can be developed by private and public entities. The information recorded in the RENAMI has a public nature.

Additionally, the Ministry of Environment has implemented the program “Huella de Carbono-Perú”, which allows public and private entities to be officially recognized for efforts in reducing greenhouse gas emissions, by means of the measurement and reporting of actions to reduce and/or neutralize them. The information contained in this program has a public nature.

Finally, the Superintendence of the Securities Market issues a report that consolidates all the information provided by issuers in the Consolidated Sustainability Report.

13. Has Peru developed a Taxonomy related to ESG?

There is no ESG related taxonomy in Peru.

14. What does the future hold for ESG in Peru?

In our view, Peru will continue to follow global trends and demands in respect of ESG matters. In the short term, Peruvian authorities will continue to focus on issuing and enforcing regulations in anti-corruption, anti-bribery and anti-money laundering matters.

In the medium term, private and public companies will continue to voluntarily incorporate an ESG agenda to their businesses. This trend will include all big, medium and small companies (medium and small companies have the highest participation in the Global Reporting Initiative). This will be coupled with a continued effort to formalize the Peruvian economy, which is a major step for broadening the ESG enforcement in Peru (and to have more reliable information regarding its compliance).

In the long term, we expect the Peruvian government to generate a comprehensive ESG legal framework, which clearly sets the obligations and rights of all stakeholders in a corporate context. This will most likely be coupled with the creation of a specialized enforcement agency in ESG matters.

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SOUTH KOREA

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ENVIRONMENTAL, SOCIAL & GOVERNANCE
Law Over Borders Comparative Guide 2023

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1. How is “ESG” in South Korea defined in a corporate/commercial context, and what are its major elements?

The 2021 “K-ESG Guidelines,” released by the Ministry of Trade, Industry, and Energy (MOTIE) in Korea, define ESG as the “three key elements of corporate management to achieve sustainability that focuses on environmental management, social responsibility, and sound and transparent governance.” “Environment” includes factors that “cover the overall environmental impact of a company’s business activities, [...] carbon neutrality related to climate change and the use of renewable energy.” The “Social” prong of ESG is defined as “the rights, duties, and responsibilities of a company to various stakeholders,” including human rights issues, as well as safety and health. Under “Governance,” the K-ESG Guidelines include “the rights and responsibilities of the company’s management and board of directors, shareholders and various stakeholders of the company,” including issues of diversity of the board of directors, executive salaries, ethical management, and auditing organizations.

2. What, if any, are the major laws/regulations in South Korea specifically related to ESG?

As to the integration of ESG factors into companies’ business operations, the following legislation and regulations were recently announced:

- **Sustainability Goals.** On 5 July 2022, the Framework Act on Sustainable Development (FASD) came into effect. It specifies sustainability goals and the obligations of governments, as well as companies and citizens, to promote and achieve such goals.
- **Environmental Disclosure Obligation.** In March 2021, the Environmental Technology and Industry Support Act (ETISA) was amended to expand environmental disclosure obligations to all companies listed on the KOSPI Market Division of the Korea Exchange (KRX) (KOSPI Listed Companies) with total assets greater than or equal to KRW 2 trillion. The disclosure obligations concern:
 - environmental goals and plans;
 - development and use of certain products or services to achieve such goals and plans; and
 - a list of achievements relating to the outcome of the environmental goals and plans.
- **Governance Disclosure Obligation.** Since 2019, the KRX has required KOSPI Listed Companies with total assets greater than or equal to KRW 2 trillion on a consolidated basis to disclose corporate governance reports. Beginning with the fiscal year 2022, and by the end of said year as well as every fiscal year thereafter, this obligation will be extended to companies having more than KRW 1 trillion on a consolidated basis and eventually to KOSPI Listed Companies by 2026.
- **Disclosure Obligation on Information Protection System.** In December 2021, the Act on the Promotion of Information Security Industry was amended to oblige companies providing an information service through information networks to disclose a system to protect the information including related investment, human resources, certificates, evaluation, monitoring, and other activities.

- **Climate Change Impact Analysis.** On 25 March 2022, the Framework Act on Carbon Neutrality and Green Growth to Respond to the Climate Crisis (FACNCG) came into effect. It sets out a carbon neutrality goal to be met by 2050 and obligations on companies to perform climate change impact analyses.
- **ESG Disclosure Obligation.** On 14 January 2021, the Financial Services Commission (FSC) announced that it will:
 - encourage voluntary ESG disclosure by providing ESG guidance;
 - prepare mandatory disclosure rules relating to ESG, which will become applicable from 2025 to KOSPI Listed Companies with more than KRW 2 trillion in assets; and
 - apply such disclosure rules to all KOSPI Listed Companies from 2030.

3. What other laws/regulations in South Korea touch on ESG themes?

The Constitution of the Republic of Korea (the “Constitution”) provides ESG-related safeguards and guarantees a focus on the government’s obligation to protect human rights in relation to environmental and social issues caused by companies, through detailed laws and regulations. Pursuant to the Constitution, laws and regulations imposing ESG principles on companies were adopted as follows:

- For environmental issues:
 - Framework Act on Environmental Policy;
 - Environmental Impact Assessment Act;
 - Act on the Integrated Control of Pollutant-Discharging Facilities;
 - Act on the Control and Aggravated Punishment of Environmental Offences;
 - Environment Dispute Mediation Act;
 - Act on Liability for Environmental Damage and Relief Thereof; and
 - Act on the Allocation and Trading of Greenhouse Gas Emissions Rights regulated by Enforcement Decree of Allocation and Trading of Greenhouse Gas Emissions Rights Act.
- For social issues:
 - Serious Accident Punishment Act (SAPA);
 - Labour Standards Act;
 - Anti-Discrimination against and Remedies for Persons with Disabilities Act;
 - Act on the Protection, etc. of Fixed-term and Part-time Employees; and
 - Act on the Protection, etc. of Dispatched Workers.
- For governance issues:
 - Commercial Code;
 - Fair Trade Law (which stipulates business interference as an illegal activity, but at the same time incorporates programs for cooperative development of large companies and SMEs in the supply chain);
 - Financial Investment Services and Capital Markets Act (which obliges KOSPI Listed Companies with total assets of KRW 2 trillion or more to appoint at least one female director to the board from 2022);
 - Act on the Corporate Governance of Financial Companies;
 - Improper Solicitation and Graft Act; and
 - Act on the Management of Public Institutions (which provides that non-standing directors of public corporations and quasi-governmental institutions

shall include one person among the employees of the relevant public corporation/institution as recommended by the employee representative).

In relation to any human rights violations that cannot be addressed by the above legislation, citizens may file a lawsuit in tort law directly against companies, as well as under the Constitutional Court Act against the Korean government.

4. What, if any, litigation or enforcement activity has South Korea seen related to ESG?

Korea has both public and private enforcement mechanisms in place based on the above-described legal system addressing ESG issues.

For public enforcement, various Korean regulatory bodies, including the National Human Rights Commission of Korea, are actively enforcing environmental, social, and human rights regulations against companies.

For private enforcement, Korea is seeing a rise in ESG litigation, including human rights and climate change litigation.

Climate change litigation includes:

- On 13 March 2020 and on 13 June 2022, respectively, 19 youth activists and 62 Korean youths, including 39 individuals under the age of 5, as well as a 20-week old fetus, filed complaints in the Constitutional Court against the Korean government, alleging that the government's insufficient action on climate change violates their fundamental rights.
- On 28 September 2020, more than 60 solar power plant owners and residents near biomass plants filed a suit in the Constitutional Court against the Korean government challenging biomass subsidies on the grounds that biomass emits more carbon dioxide than coal.
- On 23 March 2022, Korean and Australian nationals, together with members of the indigenous community in the Tiwi Islands, filed an injunction against Korean investors in relation to the gas reserve off the coast of Australia, near the Tiwi Islands.

As for social issues, various proceedings have taken place or are currently pending, including, among others:

- In 2018, a global company in Korea reached a mediated settlement with an NGO group representing more than 600 ailing workers and the families of deceased workers whose ill-health allegedly stemmed from the use of chemicals in factories.
- Various legal proceedings have commenced since 2011 in relation to consumer health issues caused by humidifier sterilizer products involving more than 1,800 consumers. In 2018, some of the representatives of related companies were sentenced to criminal punishment for professional negligence which resulted in deaths. Other related proceedings are still pending.

5. What are the major non-law/regulatory drivers of ESG trends and developments in South Korea?

Soft non-binding laws

- **UN Sustainability Development Goals (the UN SDGs).** The FASD provides grounds for the operation of the sustainability committee in the government

and issuance of the annual report to promote the UN SDGs. Detailed sustainability goals in Korea (K-SDGs) were published in 2018 through a public consultation process.

- **ESG Rating.** One of the main drivers of ESG trends and developments in Korea is the Korean Corporate Governance Service (KCGS), a non-profit organisation owned by the KRX and other related entities, which establishes the codes of practice and carries out ESG evaluations, proxy analysis, and policy research. Through an annual evaluation since 2011, KCGS rates KOSPI Listed Companies in seven different levels. The rating standards are regularly updated based on international standards, including the UN SDGs and the UN Guiding Principles on Business and Human Rights (UNGP).
- **Corporates and Human Rights Guide.** In December 2021, the Korean Ministry of Justice (MOJ) published the Corporate and Human Rights Guide (CHRG) based on the UNGP and the OECD Guidelines for Multinational Enterprises (OECD Guidelines). It provides detailed guidance to companies on how to conduct human rights and environmental due diligence in different industries.

Stakeholders

One of the most active non-profit organisations in the field of ESG in Korea is KCGS, comprising members from the KRX, Korea Securities Depository, Korea Financial Investment Association, KOSDAQ, Korea Listed Companies Association, etc. KCGS, together with other international rating agencies, is driving companies' ESG activities. As of August 2022, 192 institutional investors have signed on to KCGS's Stewardship Code, including the National Pension Service (NPS) and the Korea Teachers Pension Service (KTPS).

The Korean public's awareness of ESG issues has also increased in recent years. In May 2021, a survey result showed that more than 88.3% of consumers are willing to pay a higher price for products of ESG-compliant companies (Korean Chamber of Commerce and Industry, (KCCI), '21.5).

Recently, the risk of greenwashing is significantly increasing as major financial institutions and companies voluntarily disclose their ESG commitments and information while there are no unified ESG standards. In August 2022, the Korea Financial Supervisory Service, a governmental body overseeing the sound operation of financial institutions in Korea, expressed its concern about greenwashing and announced that it will closely monitor the issuance and operation of ESG bonds to confirm whether they are in fact complying with the information disclosed to the public.

National Contact Points (NCPs)

The Korea National Contract Point (KNCP) was established in 2001 by the MOTIE in accordance with OECD Guidelines. KNCP has been active in human rights matters of Korean companies, organising fora to engage stakeholders, organising seminars, translating and distributing due diligence guides, and so on.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate?

ESG regulation in Korea is process-focused, with various disclosure obligations

imposed on companies, such as the environmental disclosure obligation, governance disclosure obligation, disclosure obligation on information protection systems, climate change impact analysis, and the ESG disclosure obligation.

Furthermore, most major Korean conglomerates are providing voluntary ESG disclosures in their annual or biannual reports following the Global Reporting Initiative (GRI), based on the matrices of double materiality and considering the materiality of financial impacts as well as environmental and social impacts. They also frequently adopt the reporting framework of the Task Force on Climate Related Financial Disclosures (TCFD) and the Sustainability Accounting Standards Board (SASB).

7. Which sectors are most impacted by ESG in South Korea? How significant is ESG investment in South Korea?

Due to Korea's high dependency on exports (and thus on the global market demand), Korea's major industries are highly sensitive to global ESG initiatives.

Private equity

In 2022, we are witnessing heightened ESG attention in the local private equity sector, as the country's major limited partners (i.e., institutional investors who arrange and invest the capital for funds), such as the NPS and Korea Development Bank, begin to evaluate ESG considerations as key requirements when selecting their general partners (i.e., those responsible for making investment decisions).

Hedge funds/asset managers

As of August 2022, approximately 57 asset managers have adopted the KCGS's Stewardship Code. In addition, some of the largest Korean asset managers have joined the TCFD.

Banks

Major financial holding companies have pledged to cut investments in fossil fuels and make their investment portfolios carbon neutral by 2050. The banking sector is currently rushing to establish in-house committees dedicated to ESG management as part of their efforts to tighten internal structures for transparent ESG management.

Small and medium-sized enterprises (SMEs)

A 2021 survey conducted by the Korea Federation of SMEs showed that 53.3% of SMEs felt that they "need[ed] to adopt ESG management," while 89.4% felt that they were not prepared to adopt ESG measures. Most SMEs are facing requests for ESG evaluations by foreign customers and larger business partners and are looking to increase their fair trade responsibility indices. A 2022 survey conducted by the KCCI showed that, among 300 domestic export companies, 52.2% of the responding companies felt that contracts and orders from customers were likely to be disrupted due to insufficient ESG management in the supply chain in the future. When asked about ESG due diligence preparedness, 77.2% of SMEs answered "low," while only 22.8% said "high."

SOUTH KOREA

Fashion industry

An increasing number of companies active in the fashion industry are eliminating plastic bags while actively promoting eco-friendly brands as part of their efforts to meet ESG guidelines. In addition, many fashion companies are establishing committees dedicated to introducing ESG policies and other measures.

Automobile industry

Korea's automobile industry is critical to achieving the government's agenda of net-zero emissions by 2050. Korea has been introducing regulations to expand eco-friendly vehicles and is already implementing its plan to introduce a total of 624 hydrogen buses on the roads of the port cities of Busan and Ulsan and the province of South Gyeongsang by 2025 as a replacement for buses with combustion engines. However, key players are facing concerns about the new government's plan to ban purchases of internal combustion engine cars by 2035, citing unease about the Korean part-makers' (mostly SMEs) ability to meet the electrification deadlines.

Energy industry

Many Korean companies active in the energy sector have been listed on the Dow Jones Sustainability Indices (DJSI), the Carbon Disclosure Project (CDP), MSCI, KCGS, and have introduced sustainability management implementation systems.

Real estate industry

To reduce carbon dioxide emissions from real estate, the Korean government implemented the Green New Deal policy starting from July 2020 in order to digitalise and promote green buildings. In the Korean real estate investment market, significant global pension funds and large management companies have presented ESG conditions to set up blind fund agreements, using ESG as a significant investment principle and strategy.

Game and video industry

Several Korean companies in the game and video industries have launched ESG committees, published voluntary ESG reports, and introduced a corporate governance charter that lays the foundation of its sustainable business operation. These efforts aim to establish sustainable business activities within the game and video industry in Korea in line with EU and U.S. standards.

8. What are the trends in South Korea regarding ESG governance?

A survey conducted by the Daeshin Economic Research Institute in June 2021 found that of the total 106 listed companies affiliated with Korea's 10 largest conglomerates, 50 of such companies had established ESG committees. Still, as there is growing concern as to whether these committees engage in any meaningful activities, it is expected that more focus will be on actual ESG activities going forward.

Specifically, the KRX's Guidance on ESG Information Disclosure and KCGS's ESG Codes of Practice require executives and board members to set companies' ESG objectives, establish company-wide governance policies that incorporate ESG

issues, and evaluate their performance on ESG issues. Furthermore, the board and management are advised to consider how best to allocate limited company resources as they seek to achieve ESG-related goals.

9. To what extent are ESG ratings or ESG benchmarks relied upon in South Korea?

ESG rating agencies

Korean conglomerates are increasingly relying upon ESG rating agencies and indices, including the KCGS, DJSI, MSCI, EcoVadis, and Sustainalytics.

ESG benchmarks

ESG benchmarks most commonly used by Korean companies include the indices established by the GRI, KCGS, EcoVadis, Sustainalytics, WEF, and World Benchmarking Alliance.

10. What is the role of the private markets versus public markets in driving ESG developments in South Korea?

ESG in Korea is mainly driven by large companies with business interests in Europe and the U.S., which seek to satisfy their investors' and clients' ESG concerns and to align their own policies with the ones already promulgated in the EU and U.S.

Private companies

Private companies in the supply chain of public companies may be indirectly impacted by the various disclosure rules explained in Question 2 above. However, as noted above, the ESG activity levels of SMEs still remain largely dependent upon the level of large companies' assistance.

Public companies

As mentioned above, KOSPI Listed Companies will be obliged to disclose their ESG reports in a phased manner, beginning in 2025. In the meantime, many public companies are introducing ESG committees to develop ESG strategies and to integrate the newest legislation into their governance schemes.

Government-owned investors

The NPS and the KTPS have amended their investment policies to strengthen ESG considerations and augment their standards for more responsible investments. The NPS recently announced plans to accord higher evaluation marks to asset managers with investment policies that incorporate ESG and corporate responsibility standards. It will also require asset managers broadly to disclose matters relating to responsible investment in their fund management reports. The KTPS announced that from 2021, it will take into account ESG-related investment policies of fund managers and their track records in shareholder activities when evaluating asset manager appointments for managing investment portfolios of Korean companies.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

Korean companies, which may be subject to disclosure rules as explained in Question 2 above, are facing difficulties keeping up with ESG agendas and management profiles adopted by larger companies in their supply chain.

In the 2022 survey by KCCI (mentioned in Question 7 above), responding companies indicated that there is a lack of internal expertise, while the burden of consulting/training costs and the lack of supply chain ESG due diligence information are considered some of the largest hurdles.

12. What information sources are most relevant for ESG considerations in South Korea?

Korea is home to a number of high-profile institutions and NGOs focused on ESG, including the KCGS, the Korea Green Foundation, and the Korea Global Compact Network. In addition, Korean companies are increasingly integrating the GRI, CDP, and TCFD into their business models.

13. Has South Korea developed a Taxonomy related to ESG?

The Ministry of Environment of Korea established a national green taxonomy (K-Taxonomy) based on the ETISA. K-Taxonomy provides the classification of green economic activities contributing to six environmental goals:

- greenhouse gas reduction;
- adaptation to climate change;
- sustainable water conservation;
- recycling;
- pollution prevention and management; and
- biodiversity conservation.

Green economic activities must comply with three principles based on preventive environmental management and social consensus:

- contribution to environmental objectives;
- absence of serious environment damages; and
- the minimum protection mechanism.

It is divided into the “Green Category,” which contains green economic activities that are essential for carbon neutrality and environmental improvement, and the “Transition Category,” which contains transitional economic activities that are necessary to reach the ultimate goal of carbon neutrality.

14. What does the future hold for ESG in South Korea?

Korean companies are racing to prepare for their annual ESG evaluations and to align their internal policies with current ESG standards suggested by various stakeholders.

Korean companies’ medium-term goals include preparation for ESG-related disclosures, given the FSC’s 2021 plan to mandate KOSPI Listed Companies to disclose their ESG reports in a phased manner.

As part of their long-term goals, we expect to see an increasing number of companies focusing on ESG-washing issues and ESG litigation, which will likely increase due to mounting public ESG disclosure. Companies may also face human rights due diligence obligations in the future, given the ongoing discussions among stakeholders concerning human rights and environment due diligence pursuant to the MOJ's CHRG.

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1. How is “ESG” in Sweden defined in a corporate/commercial context, and what are its major elements?

The overall impression is that the interest for investing in ESG-related products, services, and processes has largely increased in Sweden during the last decade. ESG has not, however, been given any consistent definition by the Swedish legislator. This is resulting in ambiguity around the exact meaning of ESG and its main components. In Swedish legislative history, the term has been recognised by the legislator as relating to how companies affect the environment and climate, social responsibility (such as human rights), employment rights, (including non-discrimination/equal treatment) as well as company governance (such as shareholder rights and compensation to senior management).

2. What, if any, are the major laws/regulations in Sweden specifically related to ESG?

There is currently no comprehensive legislation or regulation under Swedish law specifically covering ESG. CONCORD Sweden is a platform made up of 81 Swedish civil society organisations. In May 2019, their Working Group for Business & Human Rights published a position paper calling for the government to investigate the possibility of a human rights due diligence law. In 2020, a campaign bringing together civil society organisations, trade unions, and businesses was launched.

The Swedish Government has welcomed the European Commission’s initiative on a mandatory EU due diligence duty and wants to see an ambitious approach. In 2018, the Swedish Agency for Public Management (Statskontoret) proposed that the Swedish Government investigate the possibilities for statutory requirements for Swedish companies to implement human rights due diligence, at least in high-risk situations, but no such statutory requirements have been implemented.

According to the Swedish Annual Accounts Act (1995:1554), sustainability reporting is mandatory for companies that meet at least two of the following conditions:

- the average number of employees in the company during the past two financial years exceeds 250;
- the company’s reported balance sheet total for the past two financial years exceeds SEK 175 million; and
- the company’s reported net sales for the past two financial years exceeds SEK 350 million.

The sustainability report must include statements regarding environmental, social, employment, human rights and anti-corruption issues related to the development, position, results and consequences of the company’s operations. The report can either be included in the company’s annual report or issued as a separate document.

The above-mentioned requirement for sustainability reporting implements the reporting requirements set out in the so-called non-financial reporting directive (2014/95/EU). The Swedish Annual Accounts for Credit Institutions and Securities Companies Act (1995:1559) and the Swedish Annual Accounts

for Insurance Undertakings Act (1995:1560) also set out such requirements for sustainability reporting by reference to the Swedish Annual Accounts Act.

Furthermore, the Swedish Annual Accounts Act imposes a requirement for companies listed on a regulated market to issue a corporate governance report. The report can either be included in the company's annual report or issued as a separate document and must include information about, *inter alia*, the principles the company applies (apart from the ones imposed by laws and other regulations), and, if the company meets more than one of the conditions set out above, the diversity policy applied with regards to its board of directors, the goal of the policy, how the policy has been applied during the past financial year and the results of its application.

Pursuant to the EU Sustainable Finance Disclosure Regulation (Regulation (EU) 2019/2088) (SFDR), certain Swedish financial market participants (e.g., investment firms that provide portfolio management and AIFMs) and financial advisers (as applicable) must inform their investors and customers on sustainability factors. Furthermore, Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment and amending Regulation (EU) 2019/2088 ("Taxonomy Regulation") applies to certain financial market participants, listed companies, and other large publicly owned companies. It contains rules for determining when an economic activity should be considered environmentally sustainable. The European Commission has implemented certain delegated regulations, which, among other things, require investment firms providing financial advice or portfolio management to carry out a mandatory assessment of the sustainability preferences of clients.

3. What other laws/regulations in Sweden touch on ESG themes?

Environmental

The Environmental Code (1998:808) aims to promote sustainable development that will assure a healthy and sound environment for present and future generations. Examples of other relevant pieces of environmental legislation are the Ordinance concerning Environmentally Hazardous Activities and Protection of Public Health (1998:899), the Civil Protection Act (2003:778), the Flammables and Explosives Act (2010:1011), the Transport of Dangerous Goods Act (2006:263), and the Act on Measures to Prevent and Limit the Consequences of Major Chemical Accidents (1999:381).

Social

Sweden is, from an international perspective, normally seen as a country with relatively strong employment protection. There are several laws that regulate the relationship between employers and employees. However, labour market parties can, to some extent, deviate from the legislation through collective agreements. A distinctive feature of the Swedish labour market model is, therefore, the importance of collective agreements between an employer-representative organisation or an employer and trade unions. Relevant laws are, among others, the Employment Protection Act (1982:80), the Employment Co-Determination in the Workplace

Act (1976:580), the Discrimination Act (2008:567) and the Whistleblowing Act (2021:890). The Work Environment Act (1977:1160) includes regulations about the obligations of employers and others responsible for safety to prevent ill health and accidents at work.

Governance

The main Swedish law, in an administrative context, regulating anti-money laundering is the Act on Measures against Money Laundering and Terrorist Financing (2017:630). The regulation is principally based on Directive (EU) 2015/849 and is applicable to companies that operate in certain areas. The Act aims to prevent the use of companies for money laundering and terrorist financing.

Anti-corruption is widely regulated within the criminal law area, but also through the requirement to issue a sustainability report under the Swedish Annual Accounts Act.

Government pension funds and public procurement

In areas where there is a higher involvement of public interest, such as the Swedish national pension funds and public procurement, there are stricter requirements to consider sustainability. Pursuant to the legislation governing pension funds, there is an obligation to manage the fund's assets in an exemplary manner through responsible investments and responsible ownership. In the legislative history, it is specified that this means that ESG aspects must be considered.

The Swedish Public Procurement Act (2016:1145), which applies to procurements conducted by contracting authorities (public procurement), states that a contracting authority should take environmental considerations and social and labour law considerations into account in public procurement, if the nature of the procurement so justifies. The Swedish Government has requested that the Swedish Council on Legislation (Lagrådet) review a proposal for amendments to the Swedish Public Procurement Act. The implementation of the proposed amendments would lead to the current regulation being more stringent when it comes to considering the climate, environmental, human health, animal care and social and labour law aspects.

4. What, if any, litigation or enforcement activity has Sweden seen related to ESG?

There is currently no public litigation or enforcement activity specifically related to ESG, primarily as there are no specific rules creating enforceable rights in relation to ESG under Swedish law. By contrast, litigations that touch on ESG themes, such as environmental and employment litigations, are frequently seen in the Swedish court system.

5. What are the major non-law/regulatory drivers of ESG trends and developments in Sweden?

In 2015, the Swedish Government presented a national action plan to translate the UN Guiding Principles on Business and Human Rights into practical action

at the national level. The plan is meant to assist all Swedish companies in their work with human rights questions linked to their operations. With regards to the UN Sustainable Development Goals, Nasdaq has integrated this work into the sustainability tools that it offers to issuers and investors. Nasdaq has also included a general definition of the term ESG in its ESG Reporting Guide, which is a voluntary programme for public and private companies. In the guide, ESG is referred to as “a broad set of environmental, social, and corporate governance considerations that may impact a company’s ability to execute its business strategy and create value over the long term.”

Furthermore, the market for ESG-related bonds, such as green bonds, enables companies to raise capital and invest in new and existing projects with environmental benefits. To support issuers in this matter, the International Capital Market Association has issued the Green Bond Principles, which are voluntary process guidelines for issuing green bonds.

By way of illustration of a private initiative to promote ESG aspects, Nasdaq offers a network for sustainable bonds, the Nasdaq Sustainable Bond Network, which connects issuers of sustainable bonds with investors. An issuer can apply to list their securities on the Nasdaq Sustainable Bond Network and, if the bond(s) fulfil the criteria, the application is approved and the issuer can start publishing their securities on the platform.

In addition to green and sustainable bonds, green shares have also become a way for companies to mark their shares as suitable for sustainable investments. In 2021, Nasdaq launched two different markings for green shares, Nasdaq Green Equity Designation and Nasdaq Green Equity Transition Designation, which companies can apply for. Green shares are, however, still in an early stage of development, and there is no general standard for what constitutes a green share. This will likely be more standardised as EU regulation develops further.

Sustainability-linked loans are also an established financial product in Sweden, in which the interest rate or other pricing metrics of the financial arrangement are linked to the borrower’s sustainability performance measured against environmental, social, and/or governance criteria.

Regarding the involvement of institutional investors in the development of ESG-related issues, there are, as mentioned in Question 2 above, laws under which some Swedish institutional investors are required to consider certain questions before investing the fund’s assets. Furthermore, institutional investors are also governed by investment principles and policies according to which particular issues are to be taken into account in the management of the ownership stake. Since institutional investors are major shareholders in many Swedish listed companies, this becomes highly relevant for the development of ESG and sustainability awareness in the public markets.

Pursuant to the Swedish Annual Accounts Act, it is mandatory for a company to prepare a sustainability report if it meets one or more of the conditions stated in Question 2 above. Companies listed on a regulated market that also meet one or more of these conditions must also prepare a corporate governance report that includes, among other things, the diversity policy applied to the company’s board of directors. For these companies, the requirement to publish such reports also

follows from soft law regulation in the form of the Swedish Corporate Governance Code, issued by the Swedish Corporate Governance Board. The Code includes a number of rules on good corporate governance that, apart from the requirements regarding disclosure of information, must be applied on a “comply or explain” basis. For instance, the Code states that the board of directors has a duty to identify how questions regarding sustainability can affect the company’s risks and corporate opportunities.

In the wake of increasing demand for green and sustainable investments, there is an emerging concern about greenwashing. By way of example, the Swedish Financial Supervisory Authority (Finansinspektionen) has identified greenwashing as one of the largest risks in the financial sector for 2022 and it is therefore one of the five prioritised areas that the authority will review in more detail. According to a press release published in April 2022, the authority will prepare an in-depth analysis on the topic. However, the analysis is yet to be published.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

As mentioned in Question 2, some companies must prepare reports on corporate governance and sustainability, in which certain information about the company’s operations must be disclosed to the public. These reports are to be published annually and can either be included in the company’s annual report or be published separately. Pursuant to the Swedish Corporate Governance Code, listed companies must also make the information available on their website.

7. Which sectors are most impacted by ESG in Sweden? How significant is ESG investment in Sweden?

Private equity

Private equity fund managers are impacted by ESG through the Sustainable Finance Disclosure Regulation and the Taxonomy Regulation, which requires the consideration and disclosure of ESG-related matters in their operations and when marketing their products to fund investors. In July 2021, the Swedish Private Equity & Venture Capital Association published a joint sustainability report for the Swedish private equity industry, in which they reported that portfolio companies of Swedish private equity firms are ahead of public firms in some ESG respects, while lagging behind in others.

Hedge funds/asset managers

In a similar way to private equity fund managers, hedge fund managers and asset managers in Sweden are impacted by ESG through the Sustainable Finance Disclosure Regulation and the Taxonomy Regulation. Our understanding is that asset managers are integrating ESG in their operations more actively, in conformity with the general trends of focusing on ESG and due to an increased interest from their clients. According to the Swedish Investment Fund Association, 35% of

consumer investors have chosen to invest in a fund because it is sustainable. The Swedish Investment Fund Association found that the main reason why investors choose sustainable funds is primarily the opportunity to influence development towards a sustainable society, followed by the desire to avoid unethical activities. At the same time, more and more investors indicate that they choose sustainable funds because they believe they will yield a higher return. According to a survey by the European Fund and Asset Management Association, 92% of the total assets of UCITS and AIFs in Sweden, at the end of Q1 2021, were so-called SFDR Article 8 funds.

Banks

The transition necessary to reach the goals set out in the Paris climate agreement is broadly expected to involve large investments. In this context, banks and other intermediaries in the capital market are expected to play an important part by channelling capital and, therefore, influencing what resources are used for through lending and investments. This would give the intermediaries a key role in the work of accelerating private capital's contribution to the transition.

In addition to being subject to the Sustainable Finance Disclosure Regulation and the Taxonomy Regulation (as applicable), all the major Nordic banks and the Swedish Bankers' Association have signed the UN Principles for Responsible Banking.

In 2021, the Swedish Bankers' Association, which represents banks and financial institutions in Sweden and currently has 31 member banks with operations in Sweden, published a climate roadmap to zero emissions. The purpose of the roadmap is to supplement the banks' existing efforts to integrate climate aspects into their business and set milestones in respect of achieving net-zero emissions. The milestones include the banks:

- identifying their most significant positive and negative effects on society, the economy, and the environment;
- undertaking to measure the carbon footprint from their relevant financing and investment activities to calculate their own emissions and indirect emissions; and
- ensuring that strategies and goals for the Swedish operations contribute to achieving Sweden's adopted goal of net-zero emissions by 2045.

8. What are the trends in Sweden regarding ESG governance?

Pursuant to the Swedish Corporate Governance Code, identifying how sustainability issues affect a company's risks and corporate opportunities constitutes one of the board of directors' main duties. Hence, the entire board is obligated to, in a broad manner, address issues regarding sustainability. It has also become more common for companies to appoint sustainability officers.

9. To what extent are ESG ratings or ESG benchmarks relied upon in Sweden?

ESG ratings are commonly used by institutional investors and fund managers as part of investment decision-making and assessing the sustainability of investments.

Consequently, companies (above all publicly listed companies) use ESG ratings and benchmarks in peer and competitor benchmarking purposes to attract investors. The Carbon Disclosure Project, Science Based Targets Initiative, Member of Chartered Institute for Securities & Investment, Institutional Shareholder Services group of companies, and Sustainability are commonly used for these purposes.

In addition to the aforementioned third-party ESG ratings providers, and as a consequence of the demand for benchmarking ESG, the Nasdaq Nordic exchanges have, in the past few years, launched a number of ESG initiatives, one being the ESG Data Portal, launched in 2018. The database is a centralised distribution point that offers investors access to standardised ESG data from Nordic listed companies, while listed companies are offered a platform to showcase their ESG data. The data is distributed to all investor recipients of the Nasdaq equity market data feeds, predominantly investors and brokerages acting within or having exposure to the Nordic markets.

The portal captures a range of actionable environmental, social, and corporate governance data and markets itself as providing a cost-effective manner for firms to showcase their ESG efforts. ESG reporting is encouraged but not a formal requirement for companies listed at Nasdaq Nordic.

10. What is the role of the private markets versus public markets in driving ESG developments in Sweden?

In addition to the broader trends in Sweden, the development of ESG is mainly driven by participants in the public markets. As mentioned in Question 2, it is mandatory for larger companies to annually publish reports on corporate governance and sustainability. ESG-related matters must therefore always be addressed in some way by all larger companies. Many Swedish listed companies, however, do not only comply with the minimum requirements set out by law but also go further with their sustainability work, as it is often seen as eligible from an investor perspective.

According to the most recent state ownership policy, adopted in 2020, all state-owned companies must act in an exemplary manner within the area of sustainable business. This includes strategic and transparent work guided by international guidelines, Agenda 2030, and the global goals for sustainable development. This is supplemented by legislation regulating public procurement and government pension funds, which is further described in Question 2.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

Due to the lack of an unambiguous definition of ESG, the metrics become more difficult to quantify, measure, and compare in practice. Hence, individual companies can, and have to, make their own interpretation of what ESG means in a certain context.

Furthermore, there is an inherent risk of fatigue regarding monitoring and complying with ESG-related requirements because of the plethora of ESG reporting frameworks, standards, and ratings for companies to refer to.

12. What information sources are most relevant for ESG considerations in Sweden?

Various trade associations, such as the Swedish Investment Fund Association, the Swedish Securities Markets Association, and the Swedish Bankers' Association, cover trade-specific ESG aspects within their area.

There are also product-specific information sources that aim to make it easier for buyers and investors to measure, where it is difficult for them to make such assessments, the ESG risk of purchasing or investing in a specific product. Such sources are, for instance, the Morningstar Sustainability Rating for funds, BREEAM-SE for buildings, and the Nordic Swan Ecolabel and the EU Ecolabel. In addition, the ESG ratings and benchmark institutes referred to in Question 9 can serve as sources of information for ESG considerations.

13. Has Sweden developed a Taxonomy related to ESG?

Apart from the EU Taxonomy Regulation, there is no taxonomy related to ESG in the Swedish jurisdiction.

14. What does the future hold for ESG in Sweden?

In the light of the EU's climate goals and the European Commission's Green Deal, the Swedish Competition Authority (Konkurrensverket) published a statement in 2020 regarding sustainability-related issues in a competition law context. According to the statement, the authority supports the European Commission's initiative to investigate how antitrust laws can best supplement sustainability regulation to ensure that competition law does not provide unnecessary obstacles for collaborations promoting environmental considerations. The authority emphasised that the European Commission is best suited to issue guidance, or coordinate such work as this ensures uniformity in competition supervision throughout the EU and, as a result, gives companies greater predictability.

Since ESG combines a number of different objectives, it does not provide a coherent framework for investors and companies. The uncertainty can make investors more sceptical and less willing to rely on such measurements. However, it can, in the light of the European Commission's proposal for a Directive on corporate sustainability due diligence, be assumed that ESG issues will be subject to stricter regulation in the future.

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1. How is “ESG” in Switzerland defined in a corporate/commercial context, and what are its major elements?

Switzerland follows the United Nations’ definition with regard to the scope of ESG and defined sustainability goals. The focus is on diligence and reporting obligations. In Switzerland, financial institutions, commodity traders, and energy providers are the most affected industry players and, therefore, have the most specific obligations regarding ESG. The emphasis is on sustainable business, as well as diversity and equal treatment. Switzerland has always been committed to human rights and fair working conditions.

2. What, if any, are the major laws/regulations in Switzerland specifically related to ESG?

On January 1, 2021, Switzerland introduced its first complement to the Swiss Code of Obligation, compelling companies to have a certain gender representation on the board of directors and in the executive management, or to explain why the required representation has not been reached. On January 1, 2022, further complements to the Code of Obligation were made. These include:

- provisions on transparency on non-financial matters (Art. 964a – 964c; similar to the EU’s Sustainable Disclosure Regulations);
- provisions on transparency in raw material companies (Art. 964d – 964i); and
- provisions on due diligence and transparency in relation to minerals and metals from conflict-affected areas and child labour (Art. 964j – 964l), which is supplemented by a respective ordinance detailing companies’ obligation.

Further regulations are expected to come into force in 2023, including the ordinance detailing large companies’ reporting obligations on transparency on sustainability, which are based on the Task Force on Climate-Related Financial Disclosures standard.

Furthermore, Swiss-based financial institutions are, or will regularly be, directly or indirectly affected by EU regulations and directives, including for example:

- Alternative Investment Fund Managers Directive (AIFMD);
- Undertakings for Collective Investment in Transferable Securities (UCITS) Directive;
- Markets in Financial Instruments Directive (MiFID II);
- Sustainable Finance Disclosure Regulation (SFDR); and
- Insurance Distribution Directive (IDD).

3. What other laws/regulations in Switzerland touch on ESG themes?

Switzerland’s general regulations touch on ESG themes in a wider sense. Switzerland’s Anti-Money Laundering Act (AMLA) applies to a wide range of financial intermediaries (including companies outside the scope of the financial market), which ensures the combating of money laundering and terrorist financing not only for Swiss-based companies but also for companies doing business via Switzerland or with Swiss-based companies.

Furthermore, Switzerland has enacted severe anti-bribery and corruption laws. Such provisions are not only to be found in the Swiss Criminal Code but also in the Swiss Federal Act against Unfair Competition. Moreover, the latter contains further criminal provisions that companies or customers can make use of where a competitor or company has violated fair competition rules.

The purpose of the Federal Act on Cartels and other Restraints of Competition follows a similar direction. By this act, companies are compelled to fair competition in the interests of a liberal market economy.

Additionally, Switzerland has implemented several consumer protection acts. This combination provides consumers with an advantage by, for example, enabling them to claim damages against a service provider.

4. What, if any, litigation or enforcement activity has Switzerland seen related to ESG?

To date, there are practically no judgments in Switzerland with direct reference to ESG. However, the first lawsuits are already pending. The most prominent is the climate lawsuit of the “Klima Seniorinnen Schweiz” (climate seniors) against Switzerland, which is now pending before the European Court of Human Rights.

In recent years, the Swiss National Contact Point (NCP) for the OECD Guidelines for Multinational Enterprises has conducted dozens of mediation proceedings.

5. What are the major non-law/regulatory drivers of ESG trends and developments in Switzerland?

Soft non-binding laws

Switzerland is very positive about soft laws but does not force companies to apply them. In most cases, companies are offered a right of choice. For example, the ordinance detailing companies’ obligations with regard to due diligence and transparency in relation to minerals and metals from conflict-affected areas and child labour states that companies do not need to report on the matter according to the provision of the Code of Obligation and the ordinance if they do already report in accordance to an equivalent and recognised soft law (e.g., under the OECD Guidelines for Multinational Enterprises).

Stakeholders

Switzerland’s political landscape consists of various diverse parties with different objectives. However, sustainability has become relevant in almost every party. This is obviously a reflection of the public and NGOs that push for a sustainable future.

This is also reflected by retail and institutional investors. Whereas retail investors predominantly only invest in sustainable products if the promised return seems acceptable, institutional investors have started to invest in sustainable products even if the expected return is not very satisfactory.

Moreover, the “trend to sustainability” also affect companies’ corporate agendas and strategies (e.g., Net Zero; circular economy; energy reduction). Companies are more likely nowadays to commit to soft law promoting sustainability, which in turn makes them more attractive to the general public.

On the other hand, companies are affected by the government push toward sustainability and ESG in its regulations. Also, the Swiss Financial Market Supervisory Authority tracks greenwashing risks and has published guidance on preventing and combating greenwashing. However, as of now, Switzerland lacks specific regulatory requirements for sustainability-related financial products and services, which increases the risk of greenwashing. To avoid any proceedings, Swiss financial institutions may, therefore, choose to comply with EU regulations.

National Contact Point (NCPs)

The Swiss National Contact Point (NCP) for the OECD Guidelines for Multinational Enterprises promotes the observance of the Guidelines and discusses with the parties concerned all relevant issues to contribute to the resolution of any problems that might arise. This is usually done through mediation. In Switzerland, the NCP is located at the State Secretariat of Economic Affairs (SECO) at the International Investment and Multinational Enterprises unit.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

As of now, Swiss regulations do not directly prescribe ESG-related processes that companies would have to adhere to. Rather, the provisions governing ESG goals and obligations are provisions with reporting obligations, compelling companies to report on specific matters. However, Swiss law regulates the content and method by which companies have to report on these specific matters; companies are indirectly forced to implement a corresponding “measuring process” in order to fulfil their reporting obligations.

Reporting

Companies must generally make most of the reporting obligations in their annual report. However, there are also reporting obligations that force companies to prepare separate reports on an annual basis. These include, for example, the reporting obligation on non-financial matters. Nonetheless, financial intermediaries voluntarily report on a quarterly basis to keep their investors or clients up to date. The reports are published on the company’s website.

For example, the report on non-financial matters must include:

- a) a description of the business model;
- b) a description of the policies adopted in relation to the matters referred to in (a), including the due diligence applied;
- c) a presentation of the measures taken to implement these policies and an assessment of the effectiveness of these measures;
- d) a description of the main risk related to the matters referred to in (a) and how the undertaking is dealing with this risk; in particular, this description must cover risks that arise from the undertaking’s own business operations, and provided this is relevant and proportionate, that arise from its business relationships, products, or services; and
- e) the main performance indicators for the undertaking’s activities in relation to the matters referred to in (a).

7. Which sectors are most impacted by ESG in Switzerland? How significant is ESG investment in Switzerland?

Private equity/hedge funds/asset managers/bank

In the Swiss private equity sector, the risk-return rate is the most decisive criteria for an investment decision. However, there are trends that may indicate that institutional investors are foregoing a good risk-return ratio in favour of sustainability, or that sustainability is becoming an increasingly important factor in the investment decision. This is further indicated by the growing number of investments in developing countries or investments with the objective of financial inclusion. Eventually, the markets (and with that, investors) influence the decision of whether a “green” investment is more favourable than a high return on the investment. The same applies to hedge funds, asset managers, banks, and other financial institutions.

Nonetheless, all these financial institutions must comply with financial market regulations. In this respect, financial institutions must comply with various information and transparency obligations and, in some circumstances, disclose what goals their product pursues. The objective of financial market laws is to ensure that investors are well informed and that they can make informed and responsible investment decisions on their own.

Small and medium-sized enterprises (SMEs)

Most companies in Switzerland are SMEs. Therefore, Swiss regulations provide many relief measures for SMEs so that they are not unduly affected by certain reporting obligations or are affected to a lesser extent. Nonetheless, most SMEs pay great importance to ESG matters. Thus, the overall commitment to ESG in Switzerland can be described as high.

Travel and automobile industry

Switzerland might have one of the best train systems in the world. Lots of people travel to work by train or bike. In recent years, the amount of electric or hybrid cars has increased as well.

Energy industry

The promotion of sustainable energy is high on Switzerland’s agenda. Many private households have solar panels on their roofs, new constructions are not allowed to build-in oil or gas heating, and nuclear power plants shall be taken off the grid by 2050. In this regard, Switzerland introduced its Energy Strategy 2050, which contains a step-by-step plan on how Switzerland plans to get away from fossil fuels and nuclear energy over to sustainable energy. At the same time, the strategy contributes to reducing Switzerland’s energy-related environmental impact.

8. What are the trends in Switzerland regarding ESG governance?

Sustainability is at the heart of many investment decisions. Financial products with an ESG focus are showing major asset growth worldwide – a trend that is also impressively reflected in the figures in Switzerland: the market for sustainable investments has increased 17-fold since 2010.

9. To what extent are ESG ratings or ESG benchmarks relied upon in Switzerland?

ESG rating agencies

Institutional investors, asset managers, financial institutions, and other stakeholders are increasingly using ESG ratings and rankings to evaluate and measure companies' sustainability performance over time and against their peers. Specifically, the following ESG rating and ranking agencies are commonly used: Bloomberg, Refinitive, Sustainalytics, MSCI, TruValue Labs (FactSet), ISS ESG, and V.E. (formerly known as Vigeo Eiris, a subsidiary of Moody's Corporation).

ESG benchmarks

For a long time, there was no recognized ESG equity benchmark for the Swiss stock market. Today, the Swiss Performance Index (SPI) is the basis of the new ESG indices. Furthermore, certain banks have defined sector-specific sustainability criteria for their sustainable real estate products. The ESG benchmark for direct and indirect real estate investments is the Global Real Estate Sustainability Benchmark (GRESB), which analyzes and assesses ESG performance in annual evaluations.

10. What is the role of the private markets versus public markets in driving ESG developments in Switzerland?

Private companies

Consumer expectations have changed significantly in Switzerland. Consumers expect private companies to address sustainability and to develop goals and a strategy on how they plan to achieve these sustainability goals. Larger companies have committed to reducing their CO₂-emissions by sourcing electricity from renewable energy sources, sourcing local raw materials, or moving into e-mobility.

Public companies

Many Swiss public multinational companies are members of international initiatives and report according to the GRI standard or have implemented the WEF ESG reporting metrics.

Government-owned organizations

Government-owned companies from various economic sectors have committed to reducing their CO₂ footprint by, for example, replacing old oil heating systems with climate-friendly heating systems or purchasing electricity from renewable sources. Public tenders include sustainability criteria (green procurement).

ESG agenda

The Swiss Government has not issued an ESG legislative agenda but pushes self-regulation. However, there are many ESG initiatives on all levels (government, administration, politics, and private). The Swiss Government has issued the "Energy Strategy 2050" and the CSR action plan 2020-2023.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

ESG criticism is primarily triggered by the various approaches and methods used to assess sustainability. So far, the term sustainability has not been clearly defined in the financial industry and, thus, fund providers have a free hand in applying the criteria – there is no uniform standard assessment system. This lack of legal regulation means that providers can set the criteria themselves. The lack of regulation on what sustainable investments are – or are not – makes it impossible for investors who truly want to invest green to rely on ESG ratings. In this case, it must always be expected that certain criteria are not completely fulfilled or not even fulfilled at all. In addition, the ratings of the individual agencies often differ greatly from one another. In the banking business, for example, the advisory process is central. Therefore, this is one of the biggest levers for avoiding greenwashing. Thus, the Swiss Bankers Association has developed a “Guideline for the inclusion of ESG criteria in the advisory process for private clients.” This is linked to the ongoing training of employees. Individual institutions can implement the guidelines individually according to their respective size, structure, complexity, business activities, and risks. However, greenwashing is also forbidden by the law against unfair competition.

12. What information sources are most relevant for ESG considerations in Switzerland?

Depending on the industry, there are different points of contact companies could engage with to answer ESG-specific questions. For example, different departments of the Federal Council publish information regarding ESG on their website. Financial institutions can rely on the respective information published by the Swiss Financial Market Supervisory Authority or by Self-Regulatory Organisations, as well as industry associations.

13. Has Switzerland developed a Taxonomy related to ESG?

In its report of June 24, 2020, the Swiss Federal Council concluded that there is currently no need for regulation of a state taxonomy. However, further developments in the industry and internationally, particularly in the EU, will be closely monitored and included in further in-depth work.

14. What does the future hold for ESG in Switzerland?

For companies, commitment to ESG has so far been voluntary. But the pressure to comply with ESG standards will increase in the future. Due to the increased public and political interest in the topic of sustainability, ESG criteria are now increasingly being incorporated into legislation. Thus, ESG is increasingly moving from a compliance issue – in the sense of a voluntary commitment – to a legal issue. The requirements for companies to comply with ESG standards will continue to rise steadily in the future. There is a clear trend: ESG is coming faster, more comprehensively, and more forcefully than was foreseeable even a few years ago. The trend is picking up speed. A look at other European countries shows us here in Switzerland: the corporate responsibility initiative was just the beginning.

In addition, sustainable investments are increasingly becoming the norm.

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1. How is “ESG” in the United Kingdom defined in a corporate/commercial context, and what are its major elements?

Businesses operating in (or with links to) the UK have been regulated in areas falling under the ESG banner – such as anti-bribery and corruption, health and safety, environmental concerns and employment matters – for many years. Such obligations are increasingly accompanied by specific ESG- and sustainability-related requirements. Despite these developments, the UK has no coordinated legislative definition of ESG; neither from the Companies Act 2006 (Companies Act) or from the Financial Conduct Authority (FCA). In the absence of a formal definition, ESG is widely accepted to encompass a contiguous set of risks and opportunities across a mix of “hard” and “soft” law concepts.

While the “E” of ESG has received the greatest attention historically, particularly in the run-up to (and aftermath of) COP26, the COVID-19 pandemic shifted the dialogue, focusing minds and strategies on the “S”. This includes a greater focus on worker welfare, health-and-safety factors and companies’ wider relations with their stakeholders.

To date, ESG-related regulation in the UK has centred largely on disclosure and reporting requirements aimed at driving greater transparency. The UK has a particularly strong focus on climate reporting. For example, certain large companies are now required to make disclosures in line with the Task Force on Climate-related Financial Disclosures (TCFD) recommendations (see Question 2 below). That said, the UK also has a well-established regulatory landscape for other ESG-related areas. Larger companies must report their gender pay gap, and traded companies must report specific pay ratios (e.g. the difference between CEO pay and employees at the 50th percentile). There has been recent pressure to also introduce ethnicity pay gap reporting, but the government has so far rejected this proposal.

2. What, if any, are the major laws/regulations in the United Kingdom specifically related to ESG?

While the UK has no specific ESG law, multiple pieces of legislation have a significant impact on ESG.

The Companies Act includes a number of provisions designed to increase a company’s transparency in respect of ESG-related matters:

- companies must prepare an annual strategic report that describes the principal risks and uncertainties it faces and include information about environmental and employee matters;
- certain large companies must include a non-financial and sustainability information (NFSI) statement in their strategic report that contains disclosures and policies related to:
 - the company’s impact on the environment;
 - employee, social and human rights issues;
 - anti-corruption and anti-bribery matters; and
 - climate-related financial disclosures (CRFD), (which are broadly in line with the TCFD recommendations, i.e. applying TCFD to in-scope large companies); and
- companies must include a “section 172” statement in the strategic report explaining how the directors have had regard to the issues listed in section 172

of the Companies Act, which expressly bring in ESG-related considerations (such as the community and environment and the company's employees, suppliers and customers).

Various accounting regulations require disclosure of greenhouse gas (GHG) emissions, metrics and targets. Depending on the size and type of company, certain corporates must disclose their UK energy use and associated GHG emissions.

The Listing Rules require listed companies to:

- report on a “comply-or-explain” basis in line with the TCFD recommendations – the Department for Business, Energy and Industrial Strategy (BEIS) clarified that disclosures consistent with the TCFD recommendations for the Listing Rules would also meet the CRFD requirements of the NFSI statement;
- disclose (for premium-listed companies only) on a “comply-or-explain” basis whether they have applied the UK Corporate Governance Code (UKCGC) (see Question 6 below); and
- include a diversity statement in their annual reports setting out whether certain targets have been met (e.g. that 40% of the board are women, and one member is from a minority ethnic group).

The Environment Act 2021 radically transformed environmental governance in the UK. It required the government to set binding targets across the environmental sector (e.g. regarding biodiversity) and contained significant new powers to make regulations (e.g. to recall vehicles that fail to comply with emissions standards), both of which will be highly relevant to business in the coming years.

Various pieces of EU legislation – including the Sustainable Finance Disclosure Regulation (SFDR), Taxonomy Regulation, Corporate Sustainability Reporting Directive (CSRD), proposed Corporate Sustainability Due Diligence Directive (CSDDD) and proposed Carbon Border Adjustment Mechanism (CBAM) – are highly relevant to ESG. While none have been fully on-shored post-Brexit, and the government has no plans to do so, they will still be relevant to UK firms wanting to operate inside the EU or facing investor pressure to comply with greater disclosure standards. The UK government is also looking to develop domestic versions of some of these regulations, for example, via the Sustainability Disclosure Requirements (SDR) and the UK green taxonomy, which may partially align and build on learnings from the EU versions.

The government confirmed in November 2021 that it would require certain companies to publish climate-transition plans to set out how they would decarbonise by 2050. A Transition Plan Taskforce was launched to determine the “gold standard” for transition plans, and it published a draft Disclosure Framework and Implementation Guidance in November 2022, with final versions expected in summer 2023.

3. What other laws/regulations in the United Kingdom touch on ESG themes?

In addition to the legislation and regulation outlined above in Question 2, which mostly concerns “E” matters, there is a multitude of UK law concerning “S” and “G” factors, including:

- The **Bribery Act 2010**, which applies to all UK companies and directors, includes an offence where corporates fail to prevent bribery. A defence is that the company had adequate procedures to prevent bribery; it is therefore critical that such policies are in place.

- The **Proceeds of Crime Act 2002** and **Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017** create various civil and criminal offences. Detailed policies, procedures and training are therefore paramount.
- The **Modern Slavery Act 2015** contains several offences relating to slavery, human trafficking and exploitation. It also requires large businesses to publish an annual statement setting out the steps taken (and their due diligence process) to ensure slavery and human trafficking is not taking place in their supply chain or business. There have been recent moves to extend these requirements and introduce civil penalties for non-compliance.
- The **Equality Act 2010** is designed to prevent discrimination, harassment and victimisation in the workplace.
- Various **health, safety and environmental (HSE)** legislations place criminal liability on directors where an HSE offence is committed by a company due to a director's consent, connivance or neglect.
- The UK **General Data Protection Regulation** requires personal data to be processed fairly and lawfully, grants rights to data subjects with respect to the storage and handling of their data and requires consent before personal data may be processed.
- The 2022 **Online Safety Bill** will place greater responsibility on social media platforms to remove illegal material online (particularly with respect to terrorism and child sexual exploitation) and will increase the powers of the regulator, Ofcom.

4. What, if any, litigation or enforcement activity has the United Kingdom seen related to ESG?

The number of climate change-related cases is rapidly increasing.

The most common type of ESG - related litigation in the UK concerns specific projects that are perceived to have a potentially negative environmental impact via seeking a judicial review of the granted governmental approval. For instance, in 2022, Greenpeace sought a judicial review of the approval granted to Shell's plan of developing the Jackdaw North Sea gas field on the grounds that the government had failed to properly evaluate the resulting emissions. This claim is ongoing at the time of writing.

Climate change litigation is also being conducted against the government in respect of its own policies, following the landmark decision of the Dutch Supreme Court in *State of the Netherlands v. Urgenda Foundation*. In 2022, Friends of the Earth challenged the UK government's Net Zero Strategy on the basis that it would not meet the government's net zero target. The claim succeeded, requiring the government to propose a more detailed strategy.

Activist shareholders have brought claims against companies to encourage them to take action in respect of ESG issues. In the first UK case to attempt to hold directors personally liable, ClientEarth has brought a claim against Shell's directors, arguing that they have breached their section 172 duty to promote the long-term success of the company by not taking proper action in respect of climate change.

The recent cases of *Okpabi v. Royal Dutch Shell Plc* and *Vedanta Resources PLC v. Lungowe* have confirmed that courts will take a wider approach in construing whether a parent company may have a duty of care over the acts or omissions of their foreign subsidiaries. Although these judgments do not provide exhaustive guidance on when and where a parent will be under a duty of care to those impacted by their subsidiaries and suppliers, they do illustrate that a parent company that exerts, or purports to exert, significant control over the operations of a subsidiary may incur such a duty of care. Due to the pervasive nature of ESG issues, such cases emphasise that corporate groups should ensure that ESG considerations are managed in a coordinated manner across the whole of the group.

The highest profile ESG-related enforcement activity occurred in 2021 when the UK Environment Agency required Southern Water to pay a record GBP 90 million fine, following 6,971 illegal sewage discharges between 2010 and 2015. This represented both a pecuniary blow to the water company and caused significant reputational damage.

Allegations of greenwashing are also mounting as companies increasingly make environmental claims as part of their advertising strategies. Greenwashing complaints to the advertising regulator (the Advertising Standards Authority (ASA)) have risen correspondingly; for example, the ASA banned a Tesco advert in June 2022 and HSBC adverts in October 2022. To help businesses make green statements in a compliant manner, the ASA produced a checklist for advertisers. In addition, the Competition and Markets Authority (CMA) published a Green Claims Code featuring six principles to help businesses avoid greenwashing. The CMA has considered enforcement action upon breaches of its code (see Question 7 below). The FCA also recently announced a crackdown focused on greenwashing from hedge funds and private equity funds, with the aim of improving consumer confidence in their ESG claims.

5. What are the major non-law/regulatory drivers of ESG trends and developments in the United Kingdom?

Soft non-binding laws

The TCFD recommendations, which were initially voluntary but are becoming mandatory for an increasing number of companies (see Question 2 above), are driving increased ESG reporting in the UK.

The UN Sustainable Development Goals, while not strictly a reporting framework, are widely used among UK companies, which typically seek to align business activities with particular goals.

The UN Guiding Principles on Business and Human Rights (UN GPs) are also relevant to UK companies. Shortly after publication of the UN GPs in 2011, the UK government published a report to assist companies with their implementation, but there are no current plans to convert this “soft” law into a “hard” law, unlike the French duty of vigilance law or the EU CSDDD proposal.

Stakeholders

Multiple stakeholders engage with ESG issues. Shortly before COP26, PwC

interviewed consumers, employees and executives and found that consumers expect businesses to consider ESG and would discontinue relations with companies that had poor ESG practices. It also found that employees prefer to work for companies that care about the same issues as they do.

Investors are also contributing to the growth of ESG; globally, over USD 500 billion flowed into ESG-related funds in 2021. The UK government's 2021 Roadmap to Sustainable Investing stressed the importance of investor stewardship in holding companies to account for the feasibility and credibility of their net-zero commitments and their transition strategies to align their business models with a net-zero economy.

The UK Stewardship Code (UKSC), encompassing a set of principles aimed at strengthening the quality of engagement between investors and corporates, covers a number of ESG-related issues. As of September 2022, 199 investors with assets of GBP 33 trillion have become signatories and will publish annual reports setting out how they have met the UKSC's standards.

The government has also played a significant role by converting "soft" law to "hard" law and by gradually adding "teeth" (i.e. penalties for non-compliance) to ESG-related requirements. By way of example, the government has increased the application of TCFD disclosures (see Question 2 above) and released a plan to green the financial system and further embed ESG considerations into company decision-making (see Question 6 below).

National Contact Points (NCPs)

The UK has a National Contact Point (NCP) that has two key objectives: to promote the OECD Guidelines for Multinational Enterprises on responsible business conduct; and to consider complaints about such businesses' conduct. The UK NCP was peer reviewed by the OECD in December 2019 and was found to be one of the leading NCPs, having handled the most complaints and conducted extensive promotional activities.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

The majority of the laws and regulations described in Question 2 above relate to corporate disclosure, for example, disclosures required by the Companies Act and the accounting regulations.

Corporate Governance

An exception relates to corporate governance, which are the UK Corporate Governance Code (UKCGC) and Wates Principles. The UKCGC, which is mandatory for listed companies, relates to board leadership and effectiveness, audit and financial reporting and directors' remuneration. Significantly, Principle A requires boards to "promote the long-term sustainable success of the company". The voluntary Wates Principles aim to provide a framework for good corporate governance arrangements, suitable for a diverse range of companies not subject to the UKCGC. There is overlap between the codes; for example, the Wates Principles also include the UKCGC's Principle A.

Reporting

As noted in Question 2 above, the Listing Rules and Companies Act require TCFD-aligned disclosures, which should be made in the relevant company's annual report.

In an October 2021 Greening Finance policy paper, the UK government committed to updating its disclosure regime through the proposed Sustainability Disclosure Requirements (SDRs), and a consultation on the SDRs was launched in October 2022 (closing in January 2023). The proposals include sustainable investment labels ("sustainable focus", "sustainable improvers" and "sustainable impact"), consumer-facing disclosures and detailed product-level and entity-level disclosures. In addition, the Consultation also proposes naming and marketing rules with broader applicability and a general anti-greenwashing rule, as well other specific obligations on distributors.

The labelling regime is expected to be an opt-in regime, where asset managers can choose to apply the proposed labels to their products subject to meeting the relevant eligibility requirements. The FCA has to be notified of the use of any sustainable investment labels, although no regulatory approvals are required. Products that are not labelled with one of the three sustainable investment labels but use sustainability concepts need to comply with the naming and marketing rules. The FCA expects that the SDR-labelling regime will be supported by the UK Green Taxonomy, which will set out the criteria for specific activities to be considered environmentally sustainable. A consultation on the taxonomy is also expected in the near future.

The SDRs are being developed in line with the proposed ISSB framework. The International Sustainability Standards Board (ISSB) was established by the IFRS Foundation to develop a global reporting standard. Several global standard-setting organisations have already coalesced into the ISSB organisation, including the Sustainability Accounting Standards Board (SASB), the Integrated Reporting Framework and the Climate Disclosure Standards Board. Notably, the Global Reporting Initiative (GRI) has not joined but has pledged to coordinate its future activities. The ISSB standards will take a building-block approach, and include a combination of general, thematic and industry-specific requirements, to best facilitate demand across different jurisdictions and sectors. The ISSB has published and consulted on two drafts – its general requirements for disclosure of sustainability-related financial information and its reporting standards for climate-related disclosures – and aims to issue these standards by mid-2023.

7. Which sectors are most impacted by ESG in the United Kingdom? How significant is ESG investment in the United Kingdom?

A combination of factors, including COP26 in Glasgow, severe weather events (e.g. the 2022 UK heat-wave) and the Russian invasion of Ukraine, have reinforced the importance of ESG issues and the energy transition among the general population.

While the energy and financial sectors have been significantly impacted by ESG-related issues, the universal and mandatory introduction of TCFD reporting has impacted the largest companies across all sectors.

Notably, the fashion and fast moving consumer goods (FMCG) sectors have been under increased scrutiny from the CMA. The CMA announced in January 2022 that it would investigate the environmental claims made by several fashion companies (including ASOS and Boohoo). The review considered claims about specific

products and whether companies' sweeping sustainability statements might create the wrong impression. The CMA's approach reflects the issues it identified in its Green Claims Code mentioned in Question 4 above. In January 2023, the CMA confirmed its plans to initiate a similar investigation into the FMCG sector after receiving several complaints regarding green claims made by household products.

8. What are the trends in the United Kingdom regarding ESG governance?

A key trend is the increasing appointment of Chief Sustainability Officers (CSOs) by corporations. In 2022, PwC found that the number of CSO appointments is rising rapidly, with as many CSOs appointed in 2020-21 as in the prior eight years combined.

There is a spectrum of approaches to ESG governance. An increasing number of companies have ESG committees that report directly to the board. Other companies use the fully integrated model, where each item on a board agenda would include some discussion of the relevant ESG issues. There is no one-size-fits-all approach – the aim should be to embed consideration of ESG issues within the existing governance structure and to avoid ESG-related teams and issues being 'siloed'.

9. To what extent are ESG ratings or ESG benchmarks relied upon in the United Kingdom?

ESG rating agencies

While the use of ESG ratings has dramatically increased, questions about their reliability and accuracy persist. Various studies have identified that, for the same company, ESG ratings can vary wildly across different agencies due to the different evaluations of self-reported "data" using proprietary methodologies that are rarely published. Such findings have led to criticism that ESG ratings should only be viewed as opinions, not objective weightings.

The FCA is now looking to provide greater oversight through government regulation to bring ESG data and rating providers within its purview. It also suggested that a globally consistent regulatory approach should be adopted, which is in line with the International Organization of Securities Commissions' recommendations on ESG data and ratings. In the meantime, the FCA has formed a group to develop a voluntary code of conduct, and urged greater voluntary use of guidelines from the International Capital Market Association.

ESG benchmarks

ESG benchmarks compare companies' performance against their peers. While such comparisons might avoid the issues of evaluating the underlying data, the reliability of ESG benchmarks has also been questioned. In September 2022, the FCA released a letter expressing its concerns over the benchmarks and that they might not accurately describe the economic reality they purport to measure, leading to a "trust deficit".

10. What is the role of the private markets versus public markets in driving ESG developments in the United Kingdom?

Both private and public markets are driving the ESG agenda in the UK, but

a more significant factor to determine ESG engagement is sector, with some embracing ESG more than others (e.g. renewable energy and finance).

A number of companies wishing to evidence their ESG credentials have become Certified B Corporations (B Corps). This involves passing an impact assessment and embedding the commitment to, and accountability for, high standards of social and environmental performance in a company's constitutional documents to require the directors to take decisions such that the company has a material positive impact on society and the environment, taken as a whole. More than 800 UK companies of varying sizes have become B Corps, including Kin+Carta, which was the first company listed on the London Stock Exchange to achieve B Corp status.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

Significant challenges include the fragmentation and lack of good quality ESG data. While disclosure requirements and voluntary disclosures have been increasing, there remains an insufficient quantity of data, and the quality of the data produced is inconsistent. This is partly because some ESG factors are inherently hard to measure, such as the social factors of employee work-life balance and company culture, but also because companies can be reticent to disclose unflattering data, like Scope 3 emissions or diversity and inclusion data.

Where more data is forthcoming, this data may not always be robust or accessible, and there may be ongoing questions regarding credibility and reliability. The quality of data varies considerably by size of corporate, asset class and sector. Finally, the multiplicity of ESG standards and reporting frameworks provide further complications in the evaluation of a company's ESG performance and reduces the ability of investors to successfully and accurately direct capital.

A prevailing hope is that greater international standardisation, for example through the ISSB standards, reduces reporting costs and duplication.

As noted in Question 4 above, greenwashing accusations may present an ongoing challenge for companies, and the CMA, ASA and FCA have all started to examine firms' ESG-related claims more closely. The FCA is arguably not as advanced as other financial regulators internationally (e.g. Germany's BaFin, which raided DWS, and the SEC, which fined BNY Mellon USD 1.5 million in May 2022; both issues related to misleading ESG claims).

12. What information sources are most relevant for ESG considerations in the United Kingdom?

CDP (formerly the Carbon Disclosure Project) is also widely used by large companies, typically in the extractive sector, as it collects standardised information regarding climate change, the use of natural resources and commodities.

As noted above, however, there is a smörgåsbord of frameworks that companies can utilise for disclosures in their annual or sustainability reports, and there are myriad information sources (such as S&P Global) and industry bodies (e.g. for investors, the United Nations Principles for Responsible Investment (UNPRI)).

13. Has the United Kingdom developed a Taxonomy related to ESG?

The government is in the process of developing a green taxonomy (though there have been no reports of the development of a social taxonomy). As noted above, a consultation on the taxonomy is expected in the near future, but the government may be awaiting implementation of the EU taxonomy before fashioning the UK version.

14. What does the future hold for ESG in the United Kingdom?

In the near future, ESG's ubiquity is likely to continue to advance.

The UK already has mandatory ESG obligations that are more prescriptive than other countries, and further regulations, such as a green taxonomy, SDR regime, mandatory transition plans, economy-wide TCFD disclosures and plans to implement the ISSB standards, are on the horizon. Such plans, however, require political will that may instead be focussed on minimising short-term costs and ensuring security of supply.

Looking further ahead, the general public, investors and regulators will expect higher ESG standards, and UK legislation will likely follow the EU's ESG advances. Both greater standardisation and wider assurance requirements are likely.

AUTHOR BIOGRAPHIES



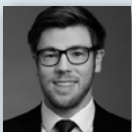
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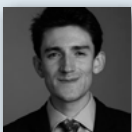
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UNITED STATES

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1. How is “ESG” in the United States defined in a corporate/commercial context, and what are its major elements?

In the United States, neither ‘ESG’ collectively nor the ‘E,’ ‘S,’ or ‘G’ individually has a singular legal definition. Nor is there a settled view in the U.S. business community as to ESG’s precise contours.

Generally, ESG is viewed as shorthand for a broad range of societal challenges that businesses are increasingly being called on to help address, posing both risks and opportunities. These issues fall under ‘environment’ (inclusive of climate change, greenhouse gas emissions, biodiversity, resource use, and preservation); ‘social’ (inclusive of diversity, equity and inclusion, racial justice, human rights, labor conditions, and labor rights); and ‘governance’ (inclusive of traditional corporate governance, board diversity and competency, bribery and corruption, and good governance).

2. What, if any, are the major laws/regulations in the United States specifically related to ESG?

2022 saw a wave of ESG-related legal developments in the United States including by the Securities and Exchange Commission (SEC), the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), the Department of Labor (DOL), and the Environmental Protection Agency (EPA). There also have been a number of significant state-level ESG developments.

On March 21, 2022, the SEC proposed rules for climate-related disclosure requirements to be added to Regulation S-K and Regulation S-X, which are applicable to all reporting issuers including both U.S. public companies and foreign private issuers. Under this proposed rule, disclosures would appear in periodic reports (e.g., 10-Ks, 20Fs, and 10-Qs) and registration statements (e.g., S-1s, S-3s, and S-4s), phasing in over time, based on a company’s filer status.

The proposed Regulation S-K amendments would require a new, separately captioned ‘Climate-Related Disclosure’ section in applicable SEC filings. The key disclosures include: material climate-related risks and impacts; greenhouse gas emissions; risk management, oversight process and corporate governance; and targets, goals, and transition plans.

The proposed Regulation S-X amendments would require line-by-line disclosure in the notes of audited financial statements of the impacts and expenditures related to severe weather events and other natural conditions, transition activities, and identified climate-related risks. (See Question 6 for a more detailed discussion of the proposed Regulation S-K and Regulation S-X amendments.)

On May 25, 2022, the SEC proposed an amendment to the current funds Names Rule, adopted in 2001, expanding its 80 percent requirement to include ESG fund names. The SEC also issued a proposed rule related to ESG disclosures of funds and fund managers that would create additional disclosure requirements in fund prospectuses, annual reports, and adviser brochures for certain registered investment advisers, advisers exempt from registration, registered investment companies, and business development companies that offer investors products that consider ESG factors in their investment processes.

On December 16, 2021 and March 30, 2022, respectively, the OCC and the FDIC issued for public comment proposed principles for climate-related financial risk management by banks with more than USD 100 billion in total consolidated assets. The proposals, which are substantially similar, set out a 'high-level framework' for managing climate-related financial risks and call for large banks to integrate climate-risk considerations in strategy and business planning.

On November 22, 2022, the U.S. Department of Labor made available final regulations addressing a fiduciary's duties under the Employee Retirement Income Security Act (ERISA) that revise and rescind portions of the Trump-era rules that had placed a chilling effect on the ability to consider ESG factors in the management and investment of US corporate retirement plan assets (e.g., pensions and 401(k) plans). The final regulations are intended to create a framework within which an ERISA fiduciary may take ESG into account in a manner that complies with ERISA, and largely track the Department's proposed regulations on the topic that were issued in October 2021. The ESG-related portion of the regulations take effect 60 days after their publication in the Federal Register on December 1, 2022.

The Uyghur Forced Labor Prevention Act (UFLPA) took effect on June 21, 2022. The UFLPA imposes restrictions related to China's Xinjiang Uyghur Autonomous Region (XUAR) including prohibiting certain imports from the XUAR and imposing sanctions on actors responsible for human rights violations in the XUAR. The UFLPA establishes a 'rebuttable presumption' that goods mined, produced, or manufactured wholly or in part in the XUAR, or produced by certain entities, are made with forced labor and therefore are prohibited for importation. In that regard, the UFLPA establishes a high burden of proof of 'clear and convincing evidence' submitted to U.S. Customs and Border Protection, that the goods were not produced using forced labor.

Relatedly, on June 17, 2022, the Forced Labor Enforcement Task Force of the Department of Homeland Security published its Strategy to Prevent the Importation of Goods Mined, Produced, or Manufactured with Forced Labor in the People's Republic of China (UFLPA Strategy). The UFLPA Strategy provides guidance to importers on the nature of due diligence and other supply chain management controls expected of importers seeking to comply with the UFLPA and the types of evidence required to rebut the presumption.

In 2022, the federal government took action to address the disproportionate impact of pollution and climate change concerns on minority and low-income communities. On May 5, 2022, the U.S. Department of Justice (DOJ) created the Office of Environmental Justice and announced a new enforcement strategy to guide DOJ attorneys pursuing environmental justice cases. On September 24, 2022, the EPA similarly established the Office of Environmental Justice and External Civil Rights to advance environmental justice and civil rights. DOJ and the EPA are expected to scrutinize air and water pollution, soil and groundwater contamination, and other environmental issues that impact minority and low-income communities.

2022 also saw a range of U.S. state-level legislative and regulatory developments, with different approaches resulting in a challenging, bifurcated landscape to navigate at the state level.

Individual states have passed what are being viewed as 'Anti-ESG' laws and regulations, coming in two forms. First are 'Anti-Boycott' Bills targeting

‘financial institutions’ that ‘boycott’ or ‘discriminate against’ companies in certain industries and that prohibit the state from doing business with such institutions or from investing the state’s assets (including pension plan assets) through such institutions. Second are ‘No ESG Investment Bills’ prohibiting the use of state funds for the purpose of ESG or social investment. Under this type of Anti-ESG Bill, the state would be prohibited specifically from investing in strategies that consider ESG factors for any purpose other than maximizing investment returns.

17 states introduced ‘Anti-ESG’ laws in 2021 and 2022. For example, the Texas Government Code Title 10, Subtitle F, Chapter 2274 (S.B. 19, enacted in 2021) requires every financial institution doing business with state and local government entities to certify that it does not have a practice, policy, guidance, or directive that ‘discriminates against a firearm entity or firearm trade association’. In addition, S.B. 19 directs state pension and school funds to divest shares they hold in financial groups that, in the government’s view, boycott firearm companies. The Texas Government Code Title 8, Subtitle A, Chapter 809 (S.B. 13, enacted in 2021) calls upon the comptroller of public accounts to ‘prepare, maintain, and provide to the permanent school fund and each statewide retirement system a list of all financial companies that boycott energy companies’. In addition, S.B. 13 directs state pension and school funds to divest shares they hold in financial groups that, in the government’s view, boycott energy companies. Texas’s comptroller announced on August 25, 2022 that 10 investment companies and 350 investment funds ‘boycott’ fossil fuel companies in the state. These companies now face possible divestment by state pension funds due to S.B. 13.

3. What other laws/regulations in the United States touch on ESG themes?

Given the breadth of ESG, numerous U.S. laws and regulations at both the federal and state levels address ESG. We highlight here only a few of the most relevant.

The Inflation Reduction Act, which was signed into law by President Biden in August 2022, is the most ambitious climate-related legislation in U.S. history. The Inflation Reduction Act includes numerous investments in climate projects such as investments in clean and renewable energy production, tax credits aimed at reducing carbon emissions, and tax credits for households to offset energy costs.

Section 1502 of the Dodd-Frank Act, as implemented by the SEC, requires all publicly listed companies to disclose their use of conflict materials, such as tantalum, gold, tin, or tungsten, sourced from the Democratic Republic of the Congo or an adjoining country if it is ‘necessary to the functionality or production’ of a product manufactured or contracted to the manufacture by the company, and the company files reports with the SEC under the Exchange Act. Under the rule, a company that uses any of the designated minerals must conduct a reasonable country-of-origin inquiry, performed in good faith and reasonably designed to determine the material’s source.

Under the U.S. Foreign Corrupt Practices Act of 1977, the DOJ and the SEC investigate and prosecute corruption internationally. The FCPA prohibits bribery of foreign officials and it also imposes certain internal controls and books and records requirements on U.S. issuers.

The U.S. Congress also has enacted and amended various environmental statutes with the aim of reducing pollution and environmental impacts by imposing

emission standards, reporting requirements, environmental management practices, and obligations to investigate and remediate contamination, including the Clean Air Act (1970 and amended in 1990), Clean Water Act (1972 and amended in 1987), the Safe Drinking Water Act (1974 and amended in 1986 and 1996), and the Comprehensive Environmental Response, Compensation, and Liability Act (1980 and amended in 1986 and 2002).

4. What, if any, litigation or enforcement activity has the United States seen related to ESG?

In March 2021, the SEC Enforcement Division created a Climate and ESG Task Force in response to increasing investor focus and reliance on climate- and ESG-related disclosure and investment. The Task Force's mandate includes:

- developing initiatives to identify proactively ESG-related misconduct;
- identifying any material gaps or misstatements in issuers' disclosure of climate risks under existing rules; and
- analyzing disclosure and compliance issues relating to investment advisers' and funds' ESG strategies.

On April 28, 2022, the Task Force brought an enforcement action, *Securities & Exchange Commission v. Vale S.A.*, 1:22-cv-02405 (E.D.N.Y.), alleging that, since 2016, Vale S.A. had manipulated multiple dam safety audits, obtained fraudulent stability certificates, and regularly misled local governments, investors, and communities about the safety of the Brumadinho dam through its disclosures. The SEC charged Vale S.A. with violating antifraud and reporting provisions of federal securities laws.

On May 23, 2022, the SEC resolved charges against BNY Mellon Investment Adviser, Inc. for misstatements and omissions about ESG considerations in making investment decisions for certain mutual funds it managed. BNY Mellon Investment Adviser, Inc. agreed to pay a USD 1.5 million penalty to settle the charges.

On November 22, 2022, the SEC entered into a settlement agreement with Goldman Sachs Asset Management, alleging that it had not consistently followed its ESG policies and procedures in connection with products marketed as ESG investments. The products together held approximately USD 725 million in assets under supervision. Goldman paid a USD 4 million penalty and did not admit or deny the alleged shortcomings.

Recent ESG-related civil litigation includes *Earth Island Institute v. BlueTriton Brands* Civil Action 21-2659 (JEB) (D.D.C. Jan. 27, 2022), in which defendant BlueTriton, a water distribution company, was accused of greenwashing. BlueTriton made affirmative statements that it was an environmentally friendly and 'sustainable' company working to prevent plastic pollution that would 'continue to support the Company's commitment to being at the forefront of sustainable water management, advancing recycling and waste reduction' and continue 'a longstanding commitment to environmental leadership'. However, according to Earth Island Institute, BlueTriton had done little to address its plastic pollution and falsely communicated to customers that recycling mitigates the environmental harm from its plastic production and usage. Earth Island Institute alleges that BlueTriton violated the District of Columbia's Consumer Protection Procedures Act, which is a consumer protection law prohibiting a wide range of deceptive and unconscionable business practices.

In addition, there is ESG-related civil litigation involving other aspects of ESG such as a case challenging a requirement that Nasdaq-listed companies have diverse boards, and if they don't, to explain why not (*Alliance For Fair Board Recruitment v. SEC*, 5th U.S. Circuit Court of Appeals, No. 21-60626).

5. What are the major non-law/regulatory drivers of ESG trends and developments in the United States?

Soft nonbinding laws

The United States has promoted the United Nations (UN) Sustainable Development Goals (SDGs), releasing a Sustainable Development Report every year. In addition, in 2021, under the Biden Administration, the United States rejoined the Paris Agreement. The United States also promotes the UN Guiding Principles on Business and Human Rights, which recognize a three-pronged approach to protecting human rights in the context of business activity.

The United States also upholds the OECD Guidelines for Multinational Enterprises (the Guidelines), a comprehensive set of recommendations for multinational enterprises to adopt in order to minimize and resolve impacts that arise from their operations in foreign jurisdictions and to encourage positive contributions to economic, social, and environmental progress, with a National Contact Point being a dispute resolution service to assist companies and stakeholders with responsible business conduct issues.

Many U.S. companies have committed voluntarily to ESG goals through international bodies. For example, a number of U.S. financial institutions are members of the Glasgow Financial Alliance for Net-Zero and the Net-Zero Banking Alliance or Net-Zero Asset Managers initiative, which means they may be subject also to the UN's Race to Zero campaign membership criteria. Through those criteria, corporations can be held to account for making progress on their climate commitments. Although not binding on the United States, the pressure to maintain memberships in international organizations may be another driver of domestic ESG trends and developments.

National Contact Points (NCPs)

The U.S. National Contact Point (USNCP) for Responsible Business Conduct is a dispute resolution and mediation resource that can support companies and stakeholders when responsible business conduct issues arise in a company's operations.

The USNCP, which is housed in the Bureau of Economic and Business Affairs of the U.S. Department of State, has three roles, to:

- promote awareness and encourage implementation of the Guidelines to business, labor, NGOs, and other members of civil society, the general public, and the international community;
- facilitate practical application of the Guidelines by bringing business and civil society together to identify potential and emerging RBC-related risks and discuss appropriate actions and responses under the Guidelines; and
- offer a 'Specific Instance' mediation process to be used when a party raises allegations against an MNE's operations.

Shareholders

As recognized by the SEC in the 2010 Guidance and its 2022 proposals, there has been, and continues to be, significant shareholder demand for climate-related disclosures. In recent years, we have seen institutional investors form investor initiatives to encourage companies to provide better information regarding the impact of climate change on their businesses.

For example, in 2019, more than 630 investors who collectively manage more than USD 37 trillion signed the Global Investor Statement to Governments on Climate Change, which urged governments to require climate-related financial reporting. This initiative became the Investor Agenda's 2021 Global Investor Statement to Governments on the Climate Crisis, which was signed by 733 global institutional investors that collectively managed more than USD 42 trillion in assets. This investor initiative demanded that governments implement a range of measures, including mandating climate risk disclosure.

According to GlobeScan's 2021 public opinion research, U.S. retail investors are increasingly concerned with ESG investments. Half of American retail investors (51%) say ESG has influenced their investments, which is up 25 points compared to 2003.

6. Are the laws, regulations and obligations highlighted in Question 2 primarily related to corporate disclosure?

Reporting

The SEC set out the current climate disclosure framework for public companies in 2010 with its interpretive guidance (2010 Guidance). The 2010 Guidance did not create specific reporting requirements for climate change or other ESG-related matters. Instead, the 2010 Guidance recommended disclosure of:

- the impact of pending or existing climate change-related legislation, regulations, and international accords;
- the indirect consequences of regulation or business trends; and
- the physical impacts of climate change. These disclosures are recommended when the above are considered 'material' to the particular public company.

As outlined in question 2 above, the SEC's March 2022 climate-related disclosure rules proposed amendments to Regulation S-K and Regulation S-X, including disclosure of:

- a) material climate-related risks and impacts;
- b) greenhouse gas emissions;
- c) risk management, oversight process, and corporate governance; and
- d) targets, goals, and transition plans.

Under (a), the proposal would require companies to describe 'climate-related risks reasonably likely to have a material impact on the registrant, including on its business or consolidated financial statements, which may manifest over the short, medium, and long term'. These climate-related risks include both physical and transition risks. Companies would need to disclose how companies determined time horizons as well as how such determination ties to the expected useful life of assets and climate-related planning processes and goals. In addition, companies would need to consider not only the direct impacts of climate change on their financial statements and business but also the indirect impacts on their 'value chains'. The

proposal would require companies to describe ‘the actual and potential impacts of any [identified] climate-related risks . . . on the registrant’s strategy, business model, and outlook’, including: the nature of the impact; time horizon for each impact; how each impact is integrated into the company’s business model, strategy, and outlook; impacts or reasonably likely impacts on financial statements; and resilience of business strategy in light of potential changes in climate-related risks.

For (b), the rule proposes mandatory disclosures for all registrants regardless of materiality regarding direct emissions from facilities owned or activities controlled by the registrant, known as Scope 1 emissions (e.g., combustion from company facilities) and indirect emissions from purchased energy (e.g., purchased electricity, heating and cooling), known as Scope 2 emissions. Disclosure of Scope 3 emissions, which are all other emissions from upstream and downstream activities (e.g., employee commuting and emissions generated by companies in which a financial institution invests) are mandatory if the emissions are ‘material’ or if the registrant has set greenhouse gas emission reduction targets that include Scope 3 emissions.

The proposal under (c) would require companies to describe ‘the [board’s] oversight of climate-related risks’ and ‘management’s role in assessing and managing climate-related risks’. Moreover, companies would be required to describe the risk identification and assessment process, the risk management process, and the integration into overall risk management.

Finally, the proposal under (d) would require companies to describe the scope and calculation of any climate-related targets or goals, progress made, and any use of carbon offsets or renewable energy credits or certificates. Moreover, companies would be required to disclose any transition plan adopted as part of its climate risk management strategy. This disclosure would include a description of the plan, relevant metrics and targets, annual updates about the transition plan (e.g., actions taken to meet goals), and how the company plans to mitigate or adapt to identified physical and transition risks.

The proposed Regulations S-X amendments would require disclosure in the notes of audited financial statements on the impact of climate-related risks on business and consolidating financial statements, including:

- financial impact metrics of negative and positive impacts on an aggregated line-by-line basis (1% line-item threshold);
- expenditure metrics of aggregate amounts expensed or capitalized in response to climate-related impacts and risks, including transition activities, climate-related targets and goals, and other mitigation activities (1% line-item threshold); and
- impact of climate on financial estimates and assumptions.

A registrant must include in its Regulation S-X disclosures the impact of any climate-related risks identified in the Regulation S-K risk management disclosure. Specifically, the disclosure must include contextual information regarding how a certain metric was derived, including descriptions of significant inputs and assumptions, as well as any policy decisions adopted by the registrant in the calculation of the metrics. This information would come within the scope of an independent, registered public accounting firm’s audit of the financials as well as a company’s internal control over financial reporting. The financial statement disclosures would need to be provided for a company’s most recently completed fiscal year and for each historical fiscal

year included in the financial statements in the filing. There is no exemption for information that is not reasonably available with respect to historical periods.

Companies subject to the California Transparency in Supply Chains Act must disclose to what extent, if any, the retailer or manufacturer:

- verifies, evaluates, and addresses the risks of human trafficking and slavery in its product supply chain;
- audits suppliers to ensure compliance with company standards;
- requires direct suppliers to certify that the supply chains for all constituent parts comply with human trafficking prohibitions enshrined in domestic law where the part is produced;
- maintains internal accountability standards and procedures in case of violation; and
- trains employees and managers with direct responsibility for supply-chain management.

Under the Nasdaq Board Matrix, since August 8, 2022, most Nasdaq-listed companies must annually disclose statistics on their board's gender, sexual-orientation, and racial/ethnic diversity. This is the first rule of its kind to be introduced by a U.S. stock exchange.

7. Which sectors are most impacted by ESG in the United States? How significant is ESG investment in the United States?

Private equity

ESG considerations are increasingly central to investments in private equity in the United States. A U.S. SIF Foundation report, published in 2020, found that one out of every three dollars under professional management in the U.S. — a total of USD 17.1 trillion — was managed according to sustainable investing strategies. (See above, Questions 2 and 6 for further details regarding the SEC's proposed rules, such as the proposed amendment to the current Names Rule and the proposed climate-related disclosure requirements, and Question 4 for enforcement.)

Banks

Fitch Ratings considers ESG to be an increasing priority for North American banks and their stakeholders. This is both due to increased social and green bond issuances as well as systemic financial risks caused by climate change. While banks themselves are not particularly high emitting, they have a large proportion of 'financed emissions', which are included in Scope 3 GHG emissions. U.S. banks are under increasing pressure to disclose their financed emissions and commit to reducing them, in some cases, by developing strategies to reduce or stop financing to clients in certain high-emitting sectors.

Fashion

As mentioned above, the proposed FSSAA would require fashion retail sellers and manufacturers to disclose their environmental and social due diligence policies.

Travel Industry

Although not U.S.-specific, more than 300 travel companies, including U.S.-based companies, signed the Glasgow Declaration on Climate Action in Tourism during

COP26, requiring them to submit a concrete and transparent plan to cut carbon emissions in half by 2030 and reach 'net zero' by 2050.

Automobile Industry

The Inflation Reduction Act, which President Biden signed into law on August 16, 2022, has significant provisions and allocates substantial funding for various initiatives supporting the further development of the electric vehicle (EV) market. These include tax credits for the purchase of new and used EVs, incentives to support the U.S. development of industries central to EV supply chains, and support for the buildout of EV charging stations, among others. In addition, the Biden Administration's American Jobs Plan includes a USD 174 billion investment in the EV market. Furthermore, in June 2022, the Biden Administration proposed new standards for a national EV charging network. Notably, the Bipartisan Infrastructure Law included an investment of USD 7.5 billion for EV charging infrastructure and more than USD 7 billion for the critical minerals supply chains necessary for batteries, components, materials and recycling. Moreover, on August 25, 2022 the California Air Resources Board approved the Advanced Clean Cars III rule, which established a year-by-year roadmap so that, by 2035, all new cars and light trucks sold in California will be zero-emission vehicles, including plug-in hybrid electric vehicles.

8. What are the trends in the United States regarding ESG governance?

In the United States, the move toward more governance-specific ESG factors appears to be primarily market driven, though regulatory agencies are increasingly imposing demands related to ESG reporting and disclosure. According to the Financial Times, the number of Chief Sustainability Officers in Fortune 500 companies grew in 2020 to 95, a 228% increase since 2011.

There is also federal support for a growing emphasis on governance factors. On November 22, 2022, the DOL introduced new rules that would expressly enable ERISA fiduciaries to consider ESG factors in their investment decisions. These considerations include governance factors such as board composition, executive compensation and transparency, and accountability in corporate decision-making as well as a corporation's avoidance of criminal liability and compliance with labor, employment, environmental, tax, and other applicable laws and regulations.

9. To what extent are ESG ratings or ESG benchmarks relied upon in the United States?

ESG rating agencies

The Big Three credit rating agencies, namely Standard & Poors, Moody's, and Fitch Ratings, were all founded in the United States. All three provide ESG-rating services. In 2022, there were increasing calls for government regulation of the ESG ratings industry, though not government action to do so.

ESG benchmarks

MSCI is a U.S.-founded finance company that created some of the most widely used ESG benchmarks and indexes.

In addition, U.S.-based Citi's 2021 ESG Report was prepared using the GRI Standards and included reporting in accordance with SASB. Moreover, Citi's reporting is guided by the Principles for Responsible Banking, the UN Global Compact, and the UN Guiding Principles on Business and Human Rights.

10. What is the role of the private markets versus public markets in driving ESG developments in the United States?

ESG agenda

There is a wide range of actors driving ESG developments in the United States. Investor and shareholder pressure has clearly influenced the SEC's climate-change disclosure guidelines and proposals.

In its 2022 Enhancement and Standardization of Climate-Related Disclosures for Investors Proposal, the SEC noted that its 2010 Guidance on climate-related reporting for public companies was in response to increasing pressure from the public and shareholders for public companies to disclose how climate change is likely to impact their business. Many companies have provided information in response to investor demand. The SEC's March 2022 climate-related disclosure proposal said that it was 'appropriate' for the SEC to consider this investor demand when designing disclosure regimes under federal securities laws.

In recent years, companies also increasingly have weighed in on sensitive social and political issues. For example, companies across the United States expressed their support for the Black Lives Matter movement through pledges to increase diversity, donations to civil rights groups, and changes in policies and practices. Dozens of U.S. companies signed letters calling for police reforms, and, on June 2, 2020, Bank of America pledged it would spend USD 1 billion over four years to address racial and economic inequality.

With respect to ESG-related shareholder proposals, there has been an overall uptick in the United States, with a more nuanced picture in terms of the support received. Influential institutions like BlackRock have been supportive of ESG proposals, while at the same time voicing reservations, particularly for proposals that were more prescriptive in nature. These factors, in addition to talk of an impending recession, seemed to reduce the overall support of shareholders in 2022. In the oil and gas industry, shareholders of fossil fuel companies, Chevron, BP, and ConocoPhillips to name a few, increasingly voted against climate-related resolutions. This decrease in shareholder support comes in the wake of disruptive events around the globe and the profits fossil fuel companies have experienced following the energy crisis and resultant high oil prices.

11. What are the major challenges in terms of compliance for companies under ESG obligations?

Although the proliferation of voluntary disclosure and reporting frameworks has increased reporting and disclosures by companies, this has also led to challenges for investors. As letters from the Vanguard Group, Inc. and the U.S. Impact Investing Alliance in 2021 highlight, this prompted inconsistent, incomparable, and unreliable information. Due to the abundance of third-party voluntary frameworks, companies

have the ability to choose under which framework they disclose and the degree of disclosure. This has led to partial disclosures that are often inconsistent year on year; the form and content of the disclosures can vary significantly. According to a 2018 study by the World Business Council for Sustainable Development, it was difficult for investors to use sustainability disclosures because of a lack of consistency and comparability. Moreover, as these third-party frameworks are voluntary, companies lack the incentives or external pressure to provide complete and adequate disclosures.

However, according to 2021 letters from the American Enterprise Institute, Heritage Foundation, and Texas Public Policy Foundation (amongst others), there is a belief that the assumptions that underpin the climate-related impact assessment were too uncertain to enable companies to determine the real risks to their businesses caused by climate change. These commenters argue that these voluntary frameworks are unnecessary as many companies already disclose climate-related risks, and these rules are more costly than the so-called 'private ordering' of climate-related disclosures.

In addition, 2021 letters from the Institute of Free Speech, West Virginia Attorney General, and Texas Public Policy Foundation argued that mandatory climate disclosure rules could violate First Amendment rights. Also contributing to the trend may be the increased willingness of fossil fuel companies to proactively put in place energy transition plans and emissions goals to preempt climate-centric shareholder resolutions.

As noted above, individual states are passing what are being viewed as 'pro-ESG' and 'anti-ESG' laws and regulations, resulting in an increasingly bifurcated landscape. The lack of a unified national strategy is causing significant complexity for businesses operating across the United States. This has been a key challenge for financial institutions where some investors are pushing for more ESG considerations in lending and the underwriting process, while some states, mainly Texas and West Virginia, are punishing firms that have such policies in place by not allowing state entities to do business with those firms. For example, the Illinois Sustainable Investing Act (2020) mandates that 'all public or government agencies involved in managing funds ... develop, publish, and implement sustainable investment policies,' whereas Senate Bill 19 in Texas requires every financial institution doing business with state and local government entities to certify that it does not 'have a practice, policy, guidance or directive that discriminates against a firearm entity or firearm trade association.'

Another challenge is the expense of complying with climate-related reporting requirements, especially in light of the SEC's proposal for detailed climate-related disclosure (see Questions 2 and 6 for more detail). A 2022 survey by the SEC found that, on average, corporate issuers are spending USD 533,000 annually on climate-related disclosures, and institutional investors are spending USD 1,372,000 annually to collect, analyze, and report climate-related data to inform their investment decisions.

12. What information sources are most relevant for ESG considerations in the United States?

There is no single information source that consolidates all the major ESG developments taking place in the United States. For federal regulatory developments, monitoring the SEC website at www.sec.gov is helpful; congressional developments can be found at www.congress.gov. Each state government has a parallel site.

Debevoise & Plimpton LLP has an ESG Resource Center, which can be found at www.debevoise.com/topics/environment-social-and-governance, and publishes an ESG Weekly Update outlining ESG developments of interest to the business community with a focus on legal and regulatory developments, accessible through the ESG Resource Center.

13. Has the United States developed a Taxonomy related to ESG?

No.

14. What does the future hold for ESG in the United States?

In the short term, there is an expected focus on disclosure and reporting and an increased effort in enforcement. The SEC is also expected to issue final rules imposing mandatory ESG disclosures for public companies, covering corporate board diversity, climate change, and cybersecurity risk governance, among other areas.

The focus on enforcement from the SEC and DOJ is also likely to increase. In 2021, the SEC hired its first senior policy advisor for climate and ESG, created a climate and ESG task force as part of its enforcement division, and directed the Division of Corporate Finance to enhance the focus on climate-related disclosures.

We are likely to see a consolidation in ESG frameworks in the medium term. The regulatory changes on the horizon are the outcome of the SEC's March 2021 proposal, which models the climate-related disclosure requirements of the Task Force for Climate-related Financial Disclosures with the aim of producing a consistent, comparable, and reliable disclosure framework.

The Biden Administration has projected a long-term commitment to ESG. In a White House press release on April 22, 2021, President Biden announced a new target for the United States to achieve a 50%-52% reduction in U.S. greenhouse gas and pollution from 2005 levels by 2030. Moreover, the Biden Administration published its 2021 long-term strategy setting out how the United States can reach its goal of net-zero emissions no later than 2050. However, the 2022 Supreme Court decision in *West Virginia v. EPA*, 597 U.S. ___ (2022) – which held that the EPA lacked authority, under the Clean Air Act, to cap greenhouse gas emissions in the manner conceived in the Clean Power Plan – will limit the options available to the Biden Administration for reaching these goals.

As mentioned above, the Inflation Reduction Act is the most ambitious climate-related legislation in U.S. history. The Inflation Reduction Act includes numerous investments in climate projects such as investments in clean and renewable energy production, tax credits aimed at reducing carbon emissions, and tax credits for households to offset energy costs. According to a White House press-release on August 23, 2022, due to the Inflation Reduction Act's investments, the United States is on track to decrease greenhouse gas emissions by about 40% below 2005 levels in 2030, therefore positioning the United States to meet President Biden's climate goals of cutting greenhouse gases by 50%-52% in 2030 and reaching net-zero by no later than 2050.

U.S. bank regulators are expected to continue their focus on climate-related risk management for financial institutions. We anticipate final guidance from the OCC, the FDIC, and possibly the Federal Reserve Board (FRB), on a standalone

or interagency basis, in the coming months, and the FRB has indicated greater focus on climate-related scenario analysis in 2023. Some state regulators are also expected to publish guidance, such as the New York Department of Financial Services, which regulates state-supervised financial institutions.

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