Addressing SESG: aligning words and actions

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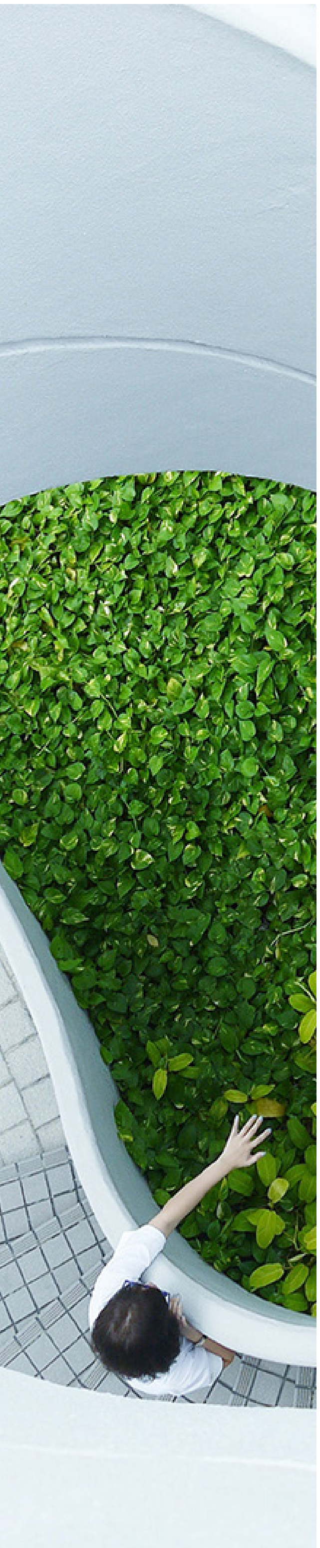
3) What is happening abroad?



Regulators around the globe are turning their focus to SESG. In early 2005, Kofi Annan, then United Nations Secretary-General, invited a group of the world's largest institutional investors to take part in developing the Principles for Responsible Investment (PRI). The PRI launched at the New York Stock Exchange that same year with 100 signatories. Today, it has more than 7,000.

Europe has been in the vanguard of the regulatory and legislative push toward SESG – for instance, see the work of the Task Force on Climate-related Financial Disclosures (TCFD), created in 2015 by the Financial Stability Board, an international body that monitors and makes recommendations about the global financial system; and the European Union's Taxonomy for Sustainable Activities. And we are confident that the US and Asia Pacific region will join this movement in 2021, with Brazil likely to follow close behind.

The move to a global corporate reporting standard for sustainability is gathering force. Recent net-zero emissions pledges from China, Japan and the Republic of Korea suggest sustainability will continue to be imperative in 2021. And early indications suggest several regulatory and legislative changes, as well as industry-level initiatives, will emerge across the Asia Pacific region in the months to come. Below we detail other developments in key jurisdictions.

CHINA: prioritizing SESG

A few years ago, making SESG-oriented investments in China presented significant challenges because data to assess Chinese companies' SESG performance was insufficient. That is rapidly changing. In 2019, 85 percent of China Securities Index 300 companies released official SESG disclosures, a significant change from 54 percent in 2013. Yet among those companies, only 12 percent provided audited reports, suggesting ample room remains for improving the quality of SESG disclosures.

A few forces are driving the trend of increasing SESG disclosure in China: (i) Chinese regulators had set a goal to mandate disclosures for listed companies by the end of 2020 (now expected to be 2021 due to the pandemic); (ii) in December 2020, President Xi Jinping announced China's goal to be carbon neutral by 2060, further pushing the transition to a low-carbon economy and likely prompting similar commitments from other global leaders; and (iii) foreign investors in Chinese assets must meet their funds' domicile standards on SESG when investing in China, driving improved reporting by Chinese firms.

In China's latest five-year plan (2021 to 2025), the country has pledged to implement the 2030 Agenda for Sustainable Development, with authorities prioritizing green improvement in the coming years.

US: Industry awaits 2021 SESG action

In 2021, investors expect SESG-related legislation from the US as part of President Joe Biden's ambitious agenda to address climate change. That agenda began to emerge in his first hours in office.[4] Within days, he had taken steps to have the US rejoin the Paris Agreement and to reimpose greenhouse gas emission limits rolled back by the Trump Administration. He also rescinded the permit for the Keystone XL pipeline and directed federal agencies to eliminate subsidies for fossil fuels "as consistent with applicable law." He also plans to direct US$2 trillion from the federal budget toward addressing climate change issues.

On December 1, 2020, another key US constituent, the Asset Management Advisory Committee of the US Securities and Exchange Commission (SEC), gathered to discuss draft recommendations proposed by its ESG Subcommittee. The subcommittee's guidelines will inform the direction of future SEC rulemaking. The draft includes several recommendations (for instance, that the SEC mandate the adoption of standards by which issuers disclose material SESG risks) and suggests best practices to enhance SESG product disclosure.

European Union: The New SESG Regulation in the EU and its applicability to third-country alternative investment fund managers

Sustainable investing and SESG are rising to the top of the agenda across the financial services industry, with a vast array of new industry bodies and initiatives both in the EU and globally. New regulations are similarly emerging to reorient capital flows toward a more sustainable economy and to enhance transparency and standardization on sustainability within the financial markets to prevent greenwashing and ensure comparability. These measures are, to date, the broadest regulatory initiatives developed in sustainable finance.

On March 10, a new regulation came into force in the EU, the Sustainable Finance Disclosure Regulation (SFDR). The SFDR requires certain firms (including private banks and wealth managers and advisers) to comply with new disclosure rules for sustainable investments and sustainability risks.

Many managers and advisers have reportedly not yet fully addressed the new requirements. DLA Piper, our global relationship partner, has prepared an overview of the main issues in SFDR implementation across Europe, including practical suggestions for addressing these issues in the *SFDR Guide*.[5]

Concerning the applicability of this new regulation to foreign entities (such as Brazilian companies), DLA Piper's *SFDR Guide* notes:

> "Apparently, this is a question even the ESAs do not have a final answer to. In their recent letter to the EU Commission, the ESAs have asked the EU Commission to clarify the extent to which SFDR applies to third-country AIFMs; for example, when marketing EU AIFs under a national private placement regime. Similar questions could arise if non-EU AIFMs manage EU AIFs or provide portfolio management or investment advice to EU AIFs. Portfolio management is defined in Art. 2 para. 6 SFDR by reference to Art. 4 para. 1 no. 8 MiFID II and covers discretionary mandates relating to financial instruments. Investment advice is defined in Art. 2 para. 16 SFDR by reference to Art. 4 para. 1 no. 4 MiFID II and covers the provision of personal recommendations on transactions relating to financial instruments. Non-EU AIFMs providing portfolio management or investment advice to EU AIFs have to fulfil the obligations for financial advisors according to Art. 2 para. 11 SFDR.
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> A number of EU fund industry associations have stated that SFDR should also apply to non-EU AIFMs if there is a nexus with the EU territory, either via the domicile of the managed or advised AIF or via the country in which marketing activities are carried out. This principle should be applied both ways, ie if an EU AIF is marketed outside the EU, the respective AIFM would still need to make the SFDR disclosures. In our opinion, since the SFDR obligations are linked to the existing EU regulatory frameworks (AIFMD, UCITSD and MiFID), the disclosure obligations under SFDR should only apply to non-EU AIFMs to the extent they are covered by the respective frameworks. Accordingly, as an example, if and to the extent the cross-border provision of portfolio management or investment advice by a non-EU AIFM does not fall under MiFID II (which is the case as long as the non-EU AIFM does not specifically solicit target clients or potential clients in the EU), the non-EU AIFM does not have to comply with SFDR."[6]

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Endnotes

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2 https://www.forbes.com/sites/tinethygesen/2017/01/24/innovation-isnt-created-the-way-people-think/?sh=6a266ffe5a8c

3 https://www.dlapiper.com/en/us/news/2020/11/dla-piper-launches-sustainability-and-esg-portal-to-help-clients-thrive-in-a-sustainable-future/

4 https://www.dlapiper.com/en/us/insights/publications/2021/01/biden-administrations-ambitious-climate-agenda-starts-now

5 https://www.dlapiper.com/en/uk/insights/publications/2021/02/sfdr-are-you-ready/

6 Ibid.

7 https://lifesciences.dlapiper.com/post/102grik/the-importance-of-an-sesg-strategy-for-life-sciences-companies

8 https://www.dlapiper.com/en/uk/insights/publications/2021/01/beyond-woke-acting-now-sesg/

9 SUSEP 2016 Sustainability Report: http://www.susep.gov.br/setores-susep/seger/codin/Ryou elatorio%20de%20Sustentabilidade%202016%20v%20final.%20docx.pdf

10 https://midias.cnseg.org.br/data/files/53/F2/D1/15/B8A6361019FF6136F98AA8A8/Declara__o%20do%20Rio.pdf

11 The rights of members of the LGBTQIA+ community are based on the principles of human dignity, equality and non-discrimination, as set out in the Federal Constitution.

12 https://dash.harvard.edu/bitstream/handle/1/14369106/15-073.pdf?sequence=1

13 https://www.dlapiper.com/en/us/news/2020/11/dla-piper-launches-sustainability-and-esg-portal-to-help-clients-thrive-in-a-sustainable-future/

14 https://treediversidade.com.br/