HERBERT SMITH FREEHILLS

ACTA Essential Treasurer: Greenwashing

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Overview

- Sustainable finance products & trends
- Greenwashing – what is it and why is an issue for corporates
- Greenwashing – relevance for sustainability financing
- Greenwashing – how to mitigate the risks

Sustainable finance products and trends

A quick snapshot of sustainable financing products

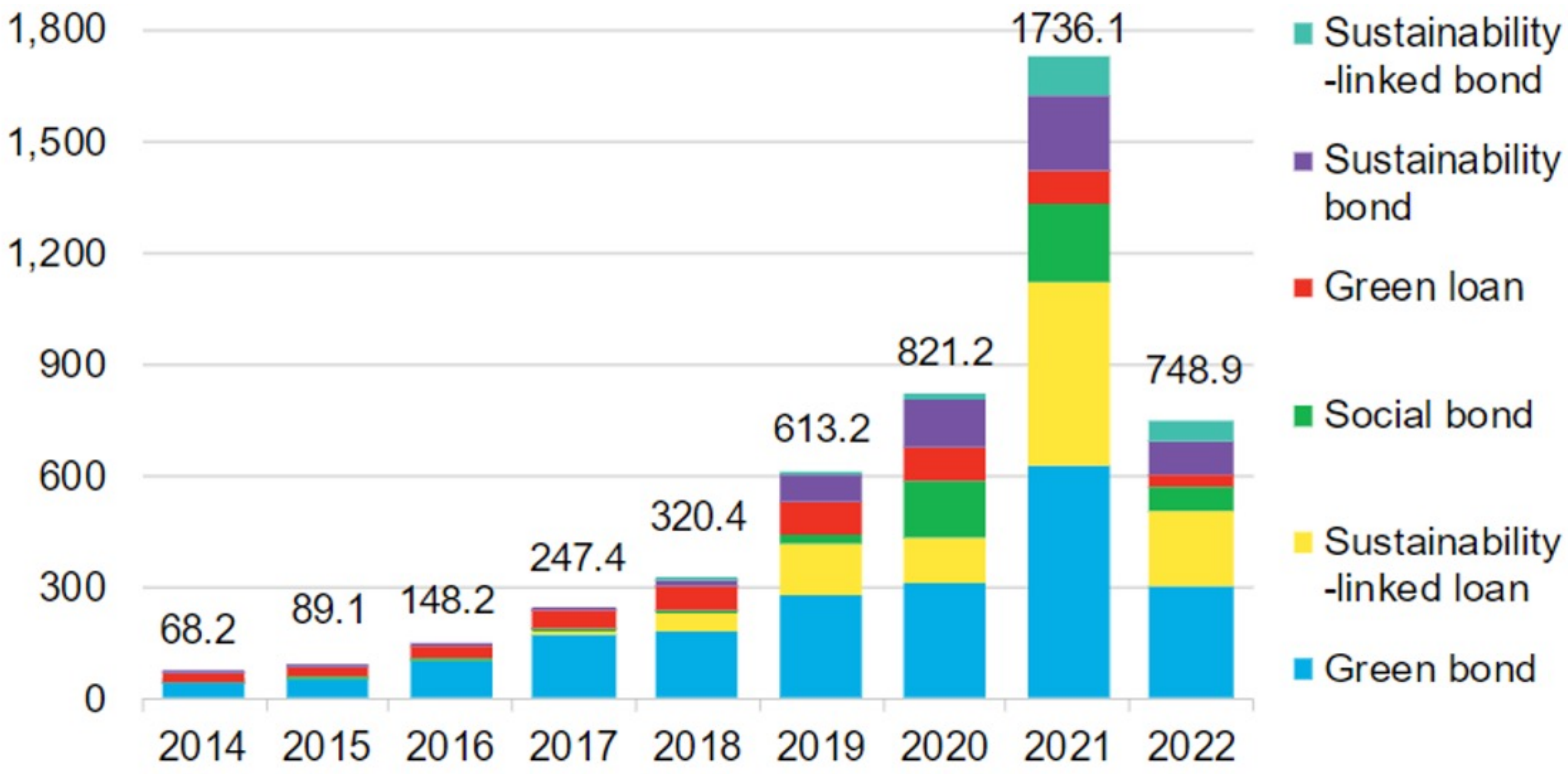
- “Use of proceeds” products
  - “green” loans/bonds
  - “social” loans/bonds
- Sustainability-linked products
  - general corporate purposes
  - incentivise achievement of pre-agreed KPIs through pricing benefits
- There is also a developing ESG-derivative market
  - ESG-linked derivatives (derivatives linked to an ESG commodity – like carbon credits)
  - Swaps with ESG KPIs leading to adjustment to premium payments

Source: BNEF Sustainable Debt Tool – February 28, 2022

Sustainable finance – global trends

The market has taken off over the past five years and become more diverse

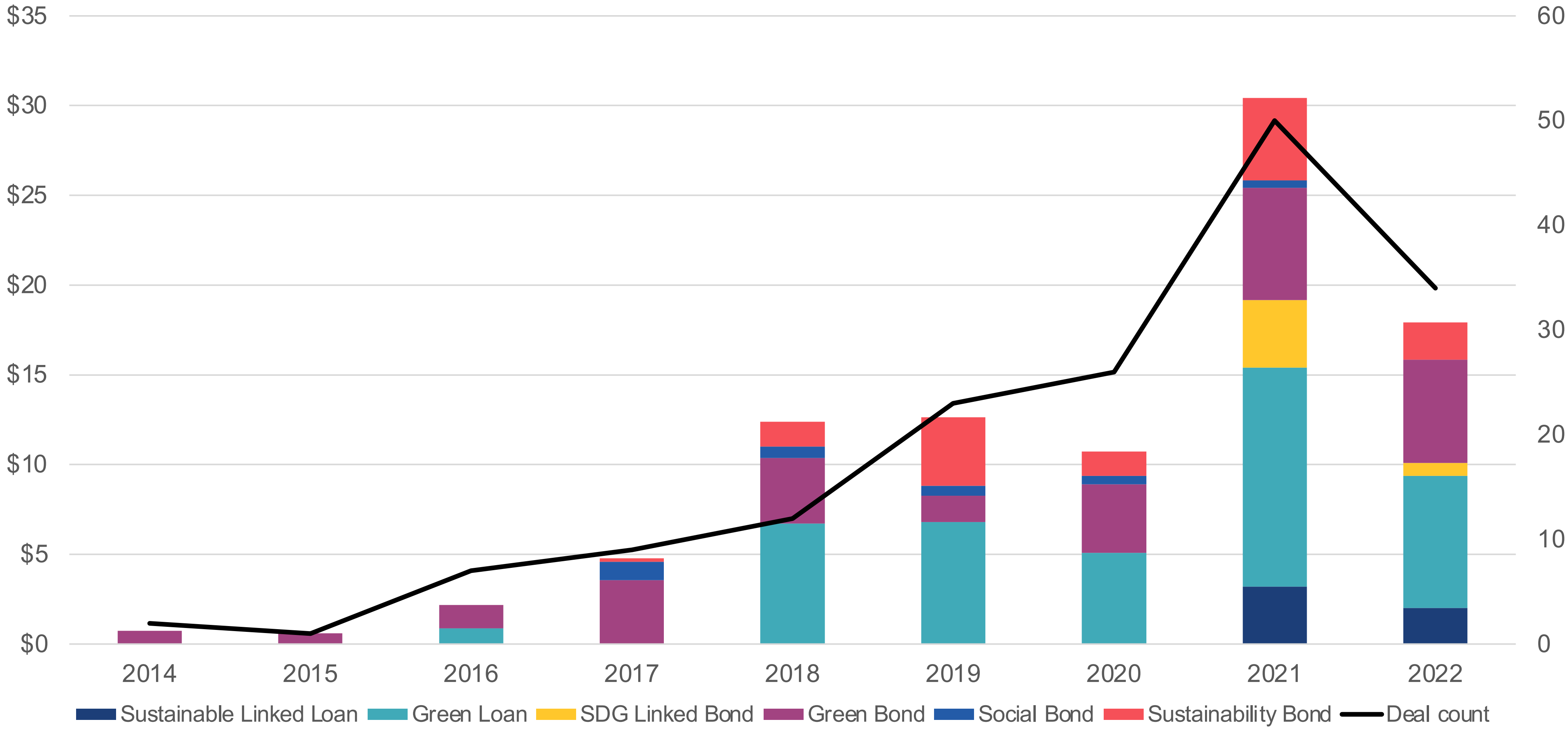
Annual sustainable debt issuance ($ billion)



Source: https://about.bnef.com/blog/sustainable-debt-issuance-dips-as-scrutiny-increases/ (graph as at 8 August 2022)

Sustainable finance – Australian trends

Australian sustainable debt issuance (A$ billion)



Source: Refinitiv

Who is driving the market for sustainable finance?

What is in it for borrowers / issuers?

- Alignment with a borrower’s ESG policies and targets
- Meeting growing investor expectations
- Positive marketing story
- Funding for sustainability improvements for existing operations or the development of new green projects
- Allows borrower to diversify its investor base
- Pricing improvements (albeit small), in the case of Sustainability Linked Loans
- Some additional transaction costs but these are outweighed by the above benefits

Greenwashing – what is it and why is an issue for corporates

What is it?

- At it’s core, greenwashing involves claims that an organisation is trying to appear “greener” than it is
- Can involve many different aspects
  - overstating environmental benefits of a product
  - statements that do not give the full story
  - making an organisation look “cleaner” by association with other organisations/products
  - misrepresenting or exaggerating a company’s commitments or actions (s247A claims)
- Not just “dirty” organisations/sectors trying to make themselves cleaner
  - “good” organisations can find themselves the subject of greenwashing allegations
  - commitments out of step with operational activities

Key area of regulatory focus

- Recent commentary from Australian regulators is consistent with increased scrutiny on greenwashing, including in the financing space
- ASIC has made this is a core strategic project in its corporate plan for 2022-26
- ACCC has misleading environmental and sustainability claims as a compliance and enforcement priority for 2022/23

> *…we are aware of growing concerns that some businesses are falsely promoting environmental or green credentials to capitalise on these consumer preferences…* Rod Sims (then ACCC Chair)

> *…we continue to monitor 'net zero' statements in both fundraising documents and in the market generally. We will take regulatory action where warranted.* … ASIC Corporate Finance Update – Issue 6

> *…with sustainability related investment growing, there is an increased risk of greenwashing…we have identified governance, transparency and disclosure standards in relation to sustainable finance as a priority for ASIC.…* ASIC Corporate Plan 2022-26

Potential liability and damage

No misleading or deceptive statements

- Overstating environmental or social benefits
- Understating environmental or social risks

Forward looking statements

- Need ‘reasonable grounds’ or may be deemed misleading if wrong
- Section 769C of the *Corporations Act 2001* (Cth)
- Section 12BB of the *ASIC Act 2001* (Cth)
- Section 4 of the *Australian Consumer Law*

Reputational

- Claims of greenwashing can have significant reputational consequences
- This can undercut the positive ESG contribution being made

An increasingly prominent issue

ASIC complaint lodged about Santos' possible 'greenwashing'

Angela Macdonald-Smith
Senior resources writer

Aug 15, 2022 – 5.00am

Activist shareholder group Market Forces has made a formal complaint to Australia's securities regulator about potentially misleading statements by Santos chairman Keith Spence and managing director Kevin Gallagher in a further escalation of climate pressures around the oil and gas producer's expansion plans.

The group has asked the Australian Securities and Investments Commission to investigate statements made by Mr Spence and Mr Gallagher at Santos' annual shareholder meeting in May

RELATED QUOTE

STO $7.9

1 year 1 day

Green groups dob in Glencore for 'greenwashing'

Elouise Fowler
Reporter

Sep 8, 2022 – 5.00am

Green groups have made a formal "greenwashing" complaint urging corporate regulators to investigate Glencore for alleged "misleading and deceptive" conduct linked to the coal miner's claims about cutting carbon emissions.

The groups have asked the Australian Consumer and Competition Commission and the Australian Securities Investment Commission to investigate 12 statements – amounting to six "misrepresentations" – by Glencore about its plans to reach net zero emissions by 2050.

Energy company fined $53,000 in ASIC's first greenwashing penalty

Hannah Wootton
Reporter

Oct 27, 2022 – 12.34pm

The corporate watchdog has slapped energy company Tlou Energy with a $53,280 fine over greenwashing, the first penalty from a major Australian regulator cracking down on this type of misconduct.

Tlou was fined over statements to the ASX last October that the electricity it produced at its Lesedi power station would produce carbon-neutral energy from the outset of its operations.

RELATED QUOTES

TOU $0.030

1 year 1 day

Greenwashing – relevance to sustainability financing

Key areas of greenwashing risk for sustainable finance

- **"Use of proceeds" products (eg green loans/bonds)**
  - no specific criteria for establishing if a project is "green"
    - potential for environmental benefits to be exaggerated
    - language matters
  - green tranche provided in a broader financing package
  - proceeds applied for different purposes (RCFs)

Key areas of greenwashing risk for sustainable finance

- **Sustainability-linked products**
  - non-ambitious targets
  - immaterial to business
  - questionable benefit
  - insufficient incentive

Similar issues arise in the "S" and "G" of ESG

Social-washing similar to greenwashing

Environmental

- Climate change and greenhouse gas (GHG) emissions
- Energy efficiency
- Resource depletion, including water
- Hazardous waste
- Air and water pollution
- Deforestation
- Biodiversity

Social

- COVID-19 response
- Human rights and modern slavery
- Underpayments
- Local and indigenous communities
- Health and safety
- Diversity and inclusion
- Workplace 'culture', bullying, harassment

Governance

- Board governance and oversight
- Risk management
- Disclosure / reporting
- Executive remuneration
- Bribery and corruption
- Data protection
- Shareholder activism
- Access to capital

An issue for financiers also

- Be aware that greenwashing is also front of mind for lenders
- Key risk areas include
  - providing finance to fossil fuel extractive sectors (in context of lender's own net zero commitments)
  - providing sustainability financing of questionable benefit
- They will also be focused on mitigating greenwashing risks

Source: BNEF Sustainable Debt Tool – February 28, 2022

Greenwashing – how to mitigate the risks

Disclosures and statements

- Disclosures particularly important when describing impact of green loans/bonds and any announcements about entering into sustainability financing products
- The risk of misleading disclosure can be managed by having an effective disclosure process, sensible disclaimers, correct framing of information, and the robust ‘testing’ of information prior to disclosure
- Some common issues for disclosures:

Definitions	Define environmental jargon (eg “clean”, “green”). Explain and, if appropriate, qualify words that are absolute.
References	Where sustainability-related metrics are used, these should be accurately described, including the source, the application, the underlying data and any risks or limitations arising from the reliance on such metrics.
Contingencies	Disclose contingencies in forward-looking statements such as the emergence of new technologies, regulatory changes or market developments.
Achievability	When discussing targets or future steps, use language based on a genuine intention, formed on reasonable grounds.
Disclaimers	Include disclaimers for forward looking statements (though, will still need to ensure statements are supported by reasonable grounds).
Alignment	Ensure statements are aligned with internal communications.

Ensure integrity of the financing

- The organisation should have a pre-existing ESG strategy – the financing should complement this
- Ensure the benefits of “green projects” are objectively identifiable and clearly communicated
- Ensure any SLL targets are relevant and ambitious:
  - tailored to the business
  - benchmarked against the sector/industry
  - a genuine stretch when measured against historical performance/trend as well as the broader sector/industry
  - encourage continued progress over time (ie cumulative targets from year to year)
  - reviewed and updated, where necessary
- Carefully consider use of ESG ratings as a KPI

External verification/certification & reporting

- For green loans/bonds, seek external input when establishing the framework and identification of relevant assets – may involve:
  - external assurance of the relevant framework
  - selection of assets by reference to external criteria (eg NABERS rating for buildings)
  - certification against external standards (eg Climate Bonds Standards)
  - reporting on use of proceeds and expected impact (and actual, if measurable)
- For sustainability-linked products, seek external input when establishing the framework and the relevant KPIs
  - external assurance of the relevant framework
  - second-party opinions as to appropriateness of the KPIs (including relevance of KPI and ambition of targets)
  - external verification and reporting of performance against standards (annually)

Adhere to guidelines

- Adhere to the relevant principles published by APLMA (for loans) or ICMA (for bonds)
- These have evolved to include features to ensure product integrity – to assist to avoid greenwashing claims
  - ICMA Green Bond Principles (updated June 2021 & June 2022)
  - APLMA Green Loan Principles (updated February 2021)
  - APLMA Sustainability Linked Loan Principles (updated March 2022)
  - APLMA Social Loan Principles (guidance released March 2022)
- Note that there are still voluntary or recommended aspects within these guidelines (eg external involvement when setting KPIs) – consider going beyond these guidelines

Disclaimer